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HUD REFORM



HEARING

BEFORE THE

SUBCOMMITTEE ON

CIS RECORD ONLY.

HOUSING AND COMMUNITY DEVELOPMENT

OF THE

**COMMITTEE ON BANKING, FINANCE AND
URBAN AFFAIRS**

HOUSE OF REPRESENTATIVES

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

OCTOBER 12, 1989

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HUD REFORM

Thursday, October 12, 1989

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON HOUSING AND COMMUNITY
DEVELOPMENT,
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS,
Washington, DC.

The subcommittee met pursuant to call at 9:30 a.m. in room 2128, Rayburn House Office Building, Hon. Henry B. Gonzalez [chairman of the subcommittee] presiding.

Present: Chairman Gonzalez, Representatives Fauntroy, Oakar, Vento, Schumer, Frank, Carper, Torres, Kennedy, Flake, Pelosi, Patterson, Hoagland, Neal, Roukema, Wylie, Hiler, Bartlett, Roth, and Saiki.

Chairman GONZALEZ. The committee will please come to order.

The Committee on Banking, Finance and Urban Affairs once again welcomes our distinguished former colleague and now Secretary of HUD, Secretary Jack Kemp in order to again hear from him.

I think the Members will recall that early after his confirmation, he not only came before our committee once, but twice, the second time with the Subcommittee on Housing, and in fact we had a full day's hearing. I believe we held on to him from about 10 o'clock to almost 5 p.m. I would like to make it eminently clear that all of us on this committee are supportive of reform in the manner in which the Department's business is conducted.

As I look at the so-called scandals that have been revealed at HUD, it is my view that we have seen a people's problem and not so much a program problem. What we have had in the last 8 years at HUD are ambitious and rather self-seeking people who betrayed public trust.

I make the distinction between scandalous mismanagement and the integrity of the HUD programs. Let me be clear. These programs work when people of good will are there to administer them. There is no way we can pass laws to make people good or to make administrators honest and efficient.

We are faced with two unnatural disasters, the swamp, as it has been aptly called, of the mismanagement at HUD and the quicksand with the housing needs that we see so sadly portrayed in the case of the homeless. The results of these two unnatural disasters are homelessness, housing that is unaffordable or nonexistent for many of our citizens.

I am pleased, Mr. Secretary, that we are hearing from you on administrative and management reforms. Many of the reforms can be

accomplished administratively or through regulatory changes, and some will require some legislation. I believe that we cannot stop at just dealing with the reforms necessary to make the Department work. We need to retool housing programs as part of a total package.

I believe that there is a strong sense of support for the reform proposals, but these must be accompanied by revitalized housing assistance programs along with new and creative approaches. We must act on reform legislation at the same time that we reauthorize a commitment to providing more affordable housing.

Mr. Secretary, on July 12, 1989, you well-stated the principle that many of us on this committee and Subcommittee on Housing hold strongly when you said, and I quote, "I did not want any of the problems at HUD to be a subterfuge for an assault on programs, people, poor people or policies that were designed to help develop the great needs of this country to house and shelter the poor and to make sure that first time home-buyers had affordable housing and we could develop our urban ghettos, boroughs, and rural communities as well."

So, Mr. Secretary, we will take you up on this statement, work cooperatively with you on enacting HUD reforms, but we also expect to enact the essential assisted housing reauthorizations. With that, I would like to recognize our preeminent minority leader of the committee, Mr. Wylie of Ohio.

Mr. WYLIE. Thank you very much, Mr. Chairman.

I think there is no doubt but that Congress and the administration must work hand in hand to clean up the problems related to mismanagement within HUD. Secretary Kemp has had to assume an unanticipated burden of fraudulent programs like hospital insurance and co-insurance, which have severely weakened the FHA insurance fund.

Problems related to favoritism, mismanagement and some ill-conceived programs have created a critical need for reform at HUD. Mr. Chairman, I know that you more than anyone are truly aware of the pressing need for reform because we have discussed it, and I would say this to your credit that you were willing to give Secretary Kemp the time and the opportunity to thoroughly evaluate the problems within his department.

Earlier this year the Secretary was before our committee, and he promised to clean up HUD from stem to stern. Well, the comprehensive reform package announced by the Secretary last week is a decisive step in that direction. The proposal addresses three major areas of concern—ethics, management and finance, and the Federal Housing Administration—in a positive way, and I think the package put forth by Secretary Kemp is truly emergency legislation.

There are some parts of it which are not all together to my liking, but I think in the overall it is a good package. We need to pass this package before we go on with major housing legislation. We must wipe the slate clean and the abuses at HUD must be cleared up first.

I am confident, Mr. Chairman, under your leadership the Banking Committee can swiftly bring a bipartisan HUD package reform bill to the House floor. You are to be commended for your patient,

thoughtful approach and your willingness to hear recommendations from our esteemed former colleague whose testimony I look forward to hearing.

Thank you very much, Mr. Chairman.

Chairman GONZALEZ. Well, thank you, Mr. Wylie.

You have stated very correctly, from the outset the 101st Congress, that you and I have pledged to work cooperatively on a bipartisan basis, which I think all through legislative history of the Congress shows that is when it works most effectively.

I would want to say something, and that is that there is some confusion in the external world, not given to our methods. The public has been reading, of course, about the hearings by the housekeeping, but nonlegislative Committee on Government Operations and the Subcommittee on Housing and Employment that has under its jurisdiction the aspect of the housing programs.

It is a nonlegislative committee, and just about a week and a half ago, I sent to each Member, and I thought the Secretary as well, a copy of a letter that I directed to Mr. Lantos, chairman of that subcommittee of Government Operations, including a copy of the report given to me by the inspector general of HUD, which was in answer to the second letter that I had referred to him a year and 3 months or so ago, the first one on June 9 and the second one on June 24.

He was replying to my June 24th request, and it had to do with the section 8 existent programs, and it was very disturbing. I referred it to Mr. Lantos so that he would continue his original set of hearings based on the inspector general's report in answer to the request we made a year ago in June, if I think the gentleman will recall, I think we also joined in that one.

So I would like to ask unanimous consent that the record of the proceedings this morning contain the letter to Mr. Lantos as well as a copy of the inspector general's report, and without objection it is so ordered.

Ms. Roukema, do you have a statement? You are the ranking Member of the Subcommittee on Housing.

Mrs. ROUKEMA. Thank you, Mr. Chairman. I appreciate your courtesy here, and I certainly want to thank Mr. Kemp for making time in his pressing schedule to meet with us so promptly. We do appreciate that and for you, Mr. Chairman, for arranging the schedule. I also wanted to stress the fact that the abuses that have come to light have been the result of examinations by other committees as well as this committee, and the hearings that you initiated and the inquiry you initiated, as you have just stated.

My sense is that we are coming to the end of the investigative phase of the scandal, at least I would hope so, and there are two more phases to follow. One, of course, is the thorough and vigorous investigation not only by HUD, but also by the Justice Department, and, Mr. Chairman, I would ask unanimous consent that some of my—the full text of my statement be included in the record, and I would like to just summarize my objections here.

Beyond the Justice Department investigation, of course, this subcommittee must consider essential legislative reforms, and the house cleaning that HUD needs, if you will. That is our responsibility.

ity, and we are the committee of authorization here: Several proposals have already been introduced.

One, of course, by the chairman of the Employment and Housing Subcommittee, Mr. Lantos. Others by Mr. Schumer of New York and one by myself. I said at the time that I introduced my bill that this is one of many proposals and that I look forward to working with my colleagues and the Secretary and his people to enact a compromise and a comprehensive bill that will deal not only effectively with the abuses and the potential abuses and corruption, but also one that will be administratively sound, not cosmetic, but faithful to our constitutional responsibilities to protect the public trust.

Mr. Chairman, I do want to say something about Secretary Kemp's outstanding efforts thus far. No Cabinet Secretary that I know has inherited a bigger, more complex set of problems. The Secretary has faced these problems admirably, squarely, and courageously, in my opinion, and has been a true public servant in the nonpartisan way he has addressed these issues.

He is going a long way towards the housecleaning that we need. I was particularly pleased to see, and we will follow up with questions today, but to see in the legislation that has been recommended by the Secretary the mandatory disclosure of consultants' activities, the sunshine, if you will, that we need to shed on this problem, strengthening the authority of the inspector general, making him a legitimate whistle-blower in the best sense of the word, and the creation of a chief official officer, a real watch dog, an official watch dog.

All of these are major provisions in a number of bills that we have discussed certainly in the Secretary's recommendations and the bill that I have cosponsored. I also would say that this is again just a first step and we must go much further in terms of providing the needed housing and the reforms and followup procedures that I am looking for the—towards the Secretary for his fine leadership.

Thank you, Mr. Secretary. Thank you, Mr. Chairman.

Chairman GONZALEZ. Thank you, Mrs. Roukema. If any other Member desires to be heard, I will be glad to recognize him briefly. If not, we will just have general leave to place in the record any prepared statements you might wish to make.

Also, without any objection, we will place your prepared text, Mrs. Roukema, in the record.

[The prepared statement of Mrs. Roukema can be found in the appendix.]

Mrs. ROUKEMA. Thank you.

Chairman GONZALEZ. I have been advised that the Assistant Secretary for Housing and FHA, Ms. Austin Fitts, has to leave here by 11:40; is that correct?

So I do welcome the help you are giving me to proceed, and we will recognize the Secretary.

Mr. VENTO. Mr. Chairman, just a brief comment in welcoming the Secretary.

I just wanted to let him know we are here and that it is better to talk to him early in the morning than later in the day.

Mr. Chairman, we appreciate the effort that the Secretary has put into the reform and his positive attitude to recognize the prob-

lems that have existed there. We also appreciate our colleagues in the Congress that are doing a thorough job of investigating with regards to the housing and the problems in HUD. That investigation goes on.

Mr. Secretary, and Mr. Chairman, one of the problems that we have, of course, is that we are talking about reframing in a fund amount, actually, some of the housing programs and assistance programs that we have.

As we know from last week's march in Washington, "Housing Now," from the renewed interest in housing and from the serious problems that are occurring with regard to the homeless, with 2 to 3 million people, it is urgent that we recast many of the housing policies that have existed in the past. And while there may be some generic issues that should be addressed in terms of reform, not just in HUD, but across the board, with regards to competitive agencies, sadly some of that effort was vetoed in the last minute of the last President's term when we tried to do some reform in a generic way.

But what I am pointing to is that I am willing to go along with some generic reforms, but I think we have to know what the programs are before we can decide in the sense what type of reforms or what type of safeguards we need. We have to know what the magnitude of the problems are, that is to say that the investigations have to be at least substantially concluded before we can do that.

I know the spirit that these are offered in is a good one, and I accept that. I just wanted to, at the onset, point out my concerns, and I want to do work in the reform.

I also want to work on the major task of addressing the housing needs we have. I hope we can go together hand-in-hand and deal with both of these problems at once, Mr. Chairman.

As you know, we have had a series of measures in. We have been bogged down with the dealing with the S&L crisis.

Now we are going to deal with reform, but I think that housing really should not be put on the back-burner. I think we owe it our best effort, and I hope that that is the spirit which prevails in this committee and within the administration.

Thank you, Mr. Chairman.

Chairman GONZALEZ. Thank you, Mr. Vento.

I had alluded to that in my statement.

Mr. Secretary, we are prepared now, and we thank you again very much. You were here very promptly at 9:30.

STATEMENT OF HON. JACK KEMP, SECRETARY, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Secretary KEMP. Thank you, Mr. Chairman.

Let me first of all thank you, Chairman Gonzalez, and your ranking Republican Member, Chalmers Wylie, and all of the members of the committee from whom, frankly, we have gotten a lot of our ideas for reform.

I don't know if there is a more bipartisan issue in the United States today than reforming this agency and making it work for people who are hurting out there in urban and, frankly, rural

American. So let me say at the outset that I can't imagine a more important task for a bipartisan consensus to work on with a sense of urgency and emergency than these reforms that come from the Congress, come from both parties, come from the IG, come from the GAO, come from our staff. The gross abuses of the past, and the empirical evidence that has been uncovered by not only the committee, Mr. Chairman, but also that of the Government Operations Committee under the chairmanship of Tom Lantos.

So I hope that my testimony today will reflect the sense of commitment that I personally feel as did my team of colleagues at HUD.

Let me for the record, Mr. Chairman, introduce Al DelliBovi, the Under Secretary, and Frank Keating, my general counsel, and Austin Fitts, our Commissioner for Housing and FHA.

Other members are here, and we have approached this with a sense of urgency and timeliness and, hopefully, bipartisanship, because I don't think it will work without that.

So that is the predicate that I would hope to lay before the committee.

As I begin my testimony let me make one other very strong statement before this committee. I did in my press conference last Tuesday, and I want to make it here on Capitol Hill. This President and this Secretary of Housing and Urban Development consider it not only a high priority, but a public good to have zero tolerance for the types of abuses that have taken place in the past.

The men and women that I have chosen and President Bush appointed, the people who have been working on this package have attempted to put the cards on the table, let the chips fall where they may. And let me say parenthetically, I think every known metaphor to human experience has been used over, and over, and over again in this effort, but from swamp to Aegean stables to just pure clearing the deck, we have approached it from a standpoint of trying to lift up the moral premise of the programs that they should touch the lives of needy people, and combat poverty and hopelessness, and homelessness and despair, and not be allowed to be ripped off by developers, or speculators, or consultants of either party. It happened in the last 8 years to be my party, and I take umbrage at those who did it.

I am as morally outraged as every single Member of your party, Mr. Chairman, and the Members of my party, including this President, want to bring it to an end, clear the decks, and get started on the great goal of bringing about a renaissance, a rebirth of our urban areas and pockets of poverty, wherever they may exist.

On July 12 before your committee I spoke of using all of our resources to bring about affordable housing and fighting poverty and help the homeless, and to implement the fair housing laws, and to encourage and incentivize the private sector to do its part, recognizing there is a public sector role; recognizing the great role that the volunteer sector, the nonprofit sector, the Jim Rouses, and the churches and synagogues can play. They are just incredible resources that we can bring to bear on this problem, notwithstanding our role at the Federal level.

I have, as I said, been very grateful for the bipartisan spirit that has been manifested in this committee.

I appreciate, Mr. Chairman, your kind remarks about our reforms, and you, too, Chalmers, and Marge, and Bruce and everybody here.

As I said, we have taken many of our ideas, frankly, from members of this committee, but I don't want to leave out GAO, or the IG, or folks who have been working with me at HUD for the last 3 months, including Lantos and Senator Moynihan and Senator Byrd, and so forth.

As you mentioned, Mr. Chairman, some of these reforms can be unilaterally implemented, some will need the cooperation of the Congress.

As you mentioned also, it is involved in three basic areas of HUD—ethics, management, and Federal Housing Administration, FHA. I am not going to go into minute detail on the more than 60 reforms that we announced, but I would like to at least briefly survey the reforms that we are calling for in those three significant areas.

Many of the problems that have existed at HUD were allowed to happen because decisions were made in the dark, decisions were made subjectively, decisions were made without a clear-cut objective. So our first effort, Mr. Chairman, was to take all of the decision-making that might be subjectively decided on a political basis, be it Republican or Democratic, and take out politics from those decisions and make sure that every community in the country, every public housing authority, every city, every mayor, every nonprofit, every contractor would know that there were rules of engagement, if you will, that there were clear, objective, definable, empirical criteria by which the decisions were to be made. And then second, to make sure that everything was done in sunshine, in the light of day, that there would be no decision at HUD that would be done by Kemp, or DelliBovi, or Keating or Fitts, or staff, or assistants or anyone, based upon influence, or who you know at HUD, or what political party you belong to, or how many consultants you hire and how much you pay them. And to the extent possible, let me assure each and every one of you, I believe with all my heart that I can appear before you as a man of candor, who served with you for many years in the Congress, and tell you flat out under my stewardship at HUD and under this President, we will remove all politics and subjectivity to the extent humanly possible from HUD.

Everything will be published in the Federal Register, every lawyer, consultant, man or women of influence who wants to do business with HUD is going to know that our decisions will be published for all to see in the Federal Register and will be based upon definable, objective criteria.

(Whereupon, at 10:05 the committee proceeded to other business)

(At 10:40 a.m., subcommittee resumed the hearing.)

Chairman GONZALEZ. The committee will please come to order.

Mr. Secretary, again we apologize and thank you at the same time for your patience.

We are now ready to give you full attention and proceed.

Secretary KEMP. Mr. Chairman, before we had to depart for urgent House responsibilities, I was responding to the need for sunshine.

I think I had made my point. I won't overdramatize it, but I want to reiterate my comment to each and every Member of the Congress, and to the President, and to everybody that our decisions will be public, and they will be published in the Federal Register.

It is no secret that waivers were being made by people deep in the bowels of our agency——

Mr. ANNUNZIO. Mr. Secretary, would you yield to me, please?

Secretary KEMP. Absolutely.

Mr. ANNUNZIO. You made a statement about notifying, everything is going to be made public. I wish you would keep in mind the Members of Congress.

As long as I have been a Member of the Congress, no department, wherever there was a grant in my city or a project, that the Congressman in that city was not notified.

I must tell you that with the previous administration, I didn't receive, and many of my colleagues did not receive, notification of what was happening in their district as far as HUD and projects were concerned.

Secretary KEMP. Well, Mr. Chairman, Mr. Annunzio, you can be assured that we want to do this up front and not only publicize the decision, but to give the reasons.

Mr. ANNUNZIO. Knowing you as well as I do, I thank you very much and I know it is going to be up front.

Secretary KEMP. If there is inside information being used by some to gain an unfair advantage for political or personal gain, I have asked for an ability to impose a civil penalty of up to \$10,000. I have suggested that every wavier at HUD will have to go through an Assistant Secretary.

In my testimony I talked about a developer on the north shore of Chicago charging rents up to \$2600 per month. It was a waiver that allowed that to happen.

So, there are such extraordinary cases of abuse of the wavier process that we are going to radically alter the way business is done. Those waivers will have to be accounted for by my assistant secretaries.

That is the impression I want to give this committee. Accountability——

Mr. ANNUNZIO. Could you make available for the record the name of the person who was granted a waiver.

Secretary KEMP. Yes. I will. I read about it in the Tribune.

[The following was subsequently received.]

The waiver in the high cost percentage was granted in 1981 by HUD's Office of Multifamily Housing Development at the request of the Chicago Area Office, to River City Developers, which was a limited partnership.

Chairman GONZALEZ. He wasn't Mr. Annunzio's constituent, that is for sure?

He couldn't be.

Mr. ANNUNZIO. If he was a constituent, I know he would be in a Federal prison. I would like the record to show the name of the man whom you are speaking about, Mr. Secretary. I would like to know if he is in prison, and what prison he is in. That is where he belongs. We are talking about \$50 million.

Secretary KEMP. And the project failed. Talk about trickle down economics, that is the most outrageous claim of helping the poor I have every heard of.

You will have all of the evidence, Mr. Chairman, for the record.

Mr. ANNUNZIO. While you are writing for the record, I would like the name of the person in your agency who granted that waiver, the name of the person.

Secretary KEMP. You will have the full IG report and all the press.

Mr. ANNUNZIO. I thank you very much.

Secretary KEMP. One other thing I hope to do, Mr. Chairman with your concurrence I would like to abandon the practice of a discretionary fund, not only in CDBG, but in every housing assistance program, so that you will know, Mr. Chairman, and your colleagues, and your party, and my colleagues will know that the Secretary is not making use of some type of a slush fund or discretionary fund.

There will be over time reasons for emergency aid to places like Charleston, SC. We will ask for a line-item appropriation for those extraordinary circumstances of a public, a disaster or for fulfilling our commitments to the civil rights laws and to our fair housing laws.

But I want that to be——

Chairman GONZALEZ. Mr. Secretary, will you yield to me at that point?

Secretary KEMP. Yes.

Chairman GONZALEZ. I want to applaud you for that. We were against granting that budgetary item. Your predecessor, though, was the first one to insist on this type of set-aside for the Secretary's discretion.

It was obvious, I guess, since 1984, 1985 particularly that some of the Members were reporting that or charging that some use of those discretionary funds were being diverted for political purposes in their areas and that they were facing opposition by some local assistant HUD officials and funds.

So I applaud that. I think that is correct.

Again, I want to express that.

Secretary KEMP. Thank you.

There are unforeseen housing problems and shortages, emergencies, desegregation efforts, but we will ask for line-item authority, and not do it through the, you know, headquarters fund.

Let me turn to management of HUD and financial reform quickly, Mr. Chairman.

It is no secret to you or your colleagues, or anybody else that there has been a woeful and inadequate management system at HUD.

One clear example comes to mind, if you can believe it. Ms. Austin Fitts has a \$300 billion portfolio and one actuary.

We are going to totally overhaul both the management and financial report system at HUD generally and in FHA specifically.

In recent testimony before your committee Mr. Bowsher of the GAO said that an important part of the solution to HUD and FHA's problems is to establish a chief financial officer.

Many members of this committee on both sides of the aisle have called—and I see Mrs. Roukema nodding her head—she is among them and others, for a chief financial officer.

I am not only going to appoint a man or woman as chief financial officer at HUD who will directly report to me and my deputy, but I am going to appoint a comptroller at FHA who will report to our commissioner and to my deputy as well as me.

We are going to make sure, sir, that we fulfill this very important responsibility that the Congress has been calling for and GAO called for.

The HUD closing agent embezzlement case is up there with the mod rehab abuses. There was no reconciling of the accounts. There was embezzlement, fraud, criminal then civil misconduct, embarrassing to the past administration at HUD. We are going to remove that lack of the accountability, require bonding, require standards, require certification of anyone who is doing business as a closing agent with HUD, and make sure we have a chief financial officer involved. I can assure you that that type of practice will not occur again to the extent that Jack Kemp has, and his team has the ability to do so.

We want to propose an amendment, Mr. Chairman, where Congress will be asked to permit more expeditious legislative review.

I recognize that that section is an important tool for oversight by your committee, the Banking Committee, and existing procedures can subject HUD to some delays.

In light of our current reform initiatives, Mr. Chairman, I think that, a lack of reform here could hinder our ability to institute the necessary policy changes and statutory mandates.

I want to increase the targeting of CDBG. These are scarce resources.

The money ought to go to fighting poverty, not building swimming pools and park benches and bike racks. I have got nothing against riding bicycles or swimming in swimming pools, but our scarce resources ought to be used to fight poverty and fulfill our commitment for affordable housing and to rehabilitate and refurbish the existing stock before we allow these precious CDBG monies to be used for anything but the low-income communities and low-income peoples that we have expressed our concern about.

So I appreciate very much, Mr. Chairman, meeting with you and talking about his, and Mr. Wylie and talking about how we can more carefully and closely target our CDBG money towards needy people, and needy communities, and fighting poverty, not allowing some of these extraneous development projects.

Therein lies, I know, a very serious question. What is development for the community and what is an anti-poverty? I just think we are going to have to use some of our own wisdom and watch this very carefully.

But I would hope we could work together to make sure CDBG is used not for big hotels, but is used for combating this terrible stain on our democracies inability heretofore to help lift people up out of poverty and get them on that ladder of self-reliance that we all acknowledge is the American dream.

We need more monitoring. I would like to have the authority to use up to half a percent of our money and programs which would be, I guess, up to \$100 million.

It wouldn't be \$100 million or more, but it would allow us to use up to that much to more closely monitor these programs and make sure they are accomplishing the goals for which they are required.

Let me turn quickly to FHA.

It is no secret that FHA needs sweeping reform. It is, as you have pointed out, and both sides agree, one of the most important ingredients in expanding the American dream of home ownership that has ever been designed. I am a strong supporter.

Austin Fitts is a strong supporter. We operate 47 different insurance programs with a portfolio of \$300 billion with, as I said, one actuary. We are going to have an independent actuarial study done to help our FHA managers assess the impact of the changing economic conditions.

Our FHA accounts were lumped together indiscriminately in the past. There has been very little accountability. We are going to put an end to that.

The one program that I wanted to end that has caused our general insurance fund serious problems was the title 10 land development scheme that allowed golf courses to be built in California and Florida. Again, I don't have anything against golf courses, but it doesn't stand the test of fighting poverty.

We asked through regulation for an end to the title 10 program. There were, I think, 53 title 10 loans. Almost half were in default. And building golf courses and swimming pools and tennis courts and health spas in California or New York or anywhere in this country just doesn't meet the test that I think you would require all of us to live up to.

So I have tried to eliminate title 10 legally through rulemaking.

Our single-family insurance program has been the cornerstone, as I suggested earlier, of our need to meet the mortgage financing needs of low- and moderate-income families and first-time home buyers. FHA was never intended to create opportunities for profits by real estate speculators.

We are asking for an end to the practice of giving FHA loans to private investors who many times walk away from these properties. I am not against private investment; I am not against the entrepreneurial capitalistic system.

But I don't want HUD and FHA to be abused to where about 2 percent of the investors in FHA policies accounted for more than 15 percent of all the losses in our single-family insurance fund.

Insurance is debatable. I happen to think that it is still a program for multifamily housing and a part of our urban strategy.

If we walk away from co-insurance, we are going to have to explain why we are going to have very little impact upon this very important need in urban America.

So I have worked with Austin and Al and Frank and my team to come up with a tightly regulated, more closely controlled and monitored co-insurance program. We have debarred, Mr. Chairman, some co-insurance lenders from doing any business with HUD. You'll be glad to know that I shut off the program. I shut it down.

We have reorganized it, reopened it, and we have barred companies like DRG from ever doing business with the Federal Government again because of the outrageous \$600 million that they have cost the American people. Worse, it was abandonment of the very legitimate program needs of helping low- and moderate-income people in urban America.

We want to stop those windfall profits by redesigning the low-income housing tax credit. It is no secret that I am a supporter of using the tax code for low-income housing and low-income economic development through enterprise zones.

We don't want people to double dip by using the low-income housing tax credit combined with the section 8 rental project driven subsidy. No one ever counted up the benefits to the developers.

We want to call into account those developers who are using subsidies along with the low-income housing tax credit and bring an end to those windfall profits so we can rest assured we are using our scarce resources for legitimate needs.

That is the end of my testimony. I am sure there are a lot of questions, Mr. Chairman. I will thank you for your patience and your support and that of both sides of the aisle.

[The prepared statement of Secretary Jack Kemp can be found in the appendix.]

Chairman GONZALEZ. Mr. Secretary, I'm going to defer to the Members who have not had that opportunity.

I did want to point out some things in fairness to some of us who have been aboard for a few years. Your recommendation that we change that requirement on the legislative days required for you to withhold the promulgation of rules or even the announcement of rules, I would like to point out that that was kind of hoisted on us.

Our minority Members, when you have a different administration administering HUD, were seeking accountability. We never really favored it. We didn't think it was a good idea to begin with. But nevertheless, the intent then was to monitor the promulgation of rules and making sure that the congressional intent would not be subverted.

With respect to your general outline intentions, I can tell you that I see no reason why you wouldn't have enthusiastic support on both sides of the aisle here. I don't think that there is any soul in or out of the Congress that doesn't realize your full integrity and honesty, purpose and performance.

Secretary KEMP. Thank you.

Chairman GONZALEZ. Mr. Wylie.

Mr. WYLIE. Thank you, Mr. Chairman. May I say the requirement on rules went into effect before I became the ranking minority Member on the committee. You looked at my direction and said something about the minority.

Chairman GONZALEZ. I looked in that direction. But actually, at that time, the minority was really in the minority status and very defensive.

The intent, you couldn't quarrel with.

Secretary KEMP. You are not suggesting, are you, Mr. Chairman, that minority is about ready to become the majority, are you?

Mr. WYLIE. Mr. Chairman, I just want to say to the Secretary that I am quite pleased with your reform package that you have been elaborating on today, and I compliment you for it. You honed in on the Community Development Block Grant targeting program and the section 8 adjustment procedures. Those procedures bother me some but not to the extent I am not ready to sign in on your package.

The Community Development Block Grant program has been used effectively and well in Columbus, OH. Mr. DelliBovi was in Columbus not long ago, and I think he will testify to that. You stated your objective is that the CDBG program should be targeted to waging a war on poverty. That was not the original intent of it, of course.

We have discussed this a little bit. But I just thought maybe you might want to elucidate for this Member on the record. I agree that it should not be used for high rise apartment buildings; but on the other hand, I think it has been used effectively in some areas, in my own city of Columbus, to revitalize the downtown area.

It was because of the discretionary aspect of it that we were able to do that, frankly.

Secretary KEMP. Coming from Buffalo, I can assure you I think CDBG has been used effectively in many cities, including Buffalo and Columbus.

I have talked to the mayors and governors. I don't think there is a whole lot of disagreement. In fact, from talking to Al DelliBovi when he got back from Columbus, and having been there myself several times, many of the things that have happened in Columbus would still on merit be encouraged under the targeted CDBG.

I want to remind everybody that statute says that the principal purpose of CDBG funding is to benefit low-and moderate-income individuals and funds should be authorized to be used in activities which aid in prevention and elimination of slums and fight poverty.

I think if we can come to some agreement about targeting a little bit better, I think we can remove what I thought and saw were some of the abuses without harming the very legitimate economic development and anti-poverty tools that we need to use from Columbus to—

Mr. WYLIE. I agree with you. I am just saying I don't think we should take away all flexibility, though, and just direct it to low-income housing.

I think that there is a problem—since we have done away with revenue sharing, as you know, some of these cities have used this as kind of a revenue sharing mechanism.

Secretary KEMP. Absolutely. I know that.

Mr. WYLIE. As I say, I had to get that in.

I agree that the FHA program is one of the greatest programs that we have ever had. It has increased funds for first-time home ownership. I was the author of the amendment which made the FHA program permanent. With the support of the chairman, we were able to get that through.

You mentioned that the report on the Federal Housing Administration cited co-insurance and hospital insurance as the two major factors contributing to problems in the general insurance fund.

Your reform package does talk about the troubled co-insurance program, but it doesn't propose changes in the hospital insurance program.

I might want to direct this to Ms. Fitts, if it is OK, to see if she is looking into that particular program.

Secretary KEMP. Absolutely.

Ms. FITTS. As you know, we have had a problem with the hospital portfolio. Approximately 50 percent of that portfolio is in New York, and there are structural problems with the hospital system, cost containment in that system, which is causing deterioration in many of those credits.

Part of the problem is that there is split responsibility on managing the program. HHS is responsible for doing the underwriting. Then we are responsible for managing the portfolio.

Currently we are in negotiations with HHS as to the best way to improve the management of this, which is why you do not see something final in this reform package because it really requires a joint effort of both agencies to solve the problem.

But we are definitely working on it and are very aware of it. It is of great concern to us.

Mr. WYLIE. I am glad I asked the question. You did not overlook it. You are just in negotiations, and you have not finalized the approach you want to take.

Secretary KEMP. We are trying to work with Dr. Sullivan at HHS to resolve this kind of a mixture that just doesn't work the way it should.

Mr. WYLIE. That makes a lot of sense. This may be a premature question, but we are under heavy pressure to increase the mortgage limits on FHA. The Ohio Homebuilders are opposed to increasing the limits on FHA. There are other areas of the country which may need the increase for the program to work better. I don't know.

Have you looked into that yet? Have you taken a position on what you recommend?

Secretary KEMP. To all of the Members who care about this FHA ceiling issue, you saw what the Senate did when they, in the Nickles amendment to the HUD appropriation bill raised the ceiling to 125 thousand dollars. It hasn't been raised in a while.

There is a necessity to raise it. We are having a full audit of the circumstances and area real estate markets that would require an adjustment. So we have favored the adjustment.

I didn't particularly think that that was the vehicle by which it should be done. I would have preferred to wait until the audit were—was done, and we had more information, and then we could act in a more prudent way.

I don't want to accuse anybody of acting imprudently, but I thought it should be done at a later time on a more logical vehicle. I did not favor, frankly, having looked at the issue from both sides and trying to objectively determine where we thought it should go, I didn't agree with the idea of taking it up to one hundred and what, 60 or 65, 165,000, because I thought that might trespass on the private sector, that it might be too high, that it might turn the program away from its original intention.

I know the good reasons for doing so. I guess I came down on the side of indexing it so that we would have a more objective criterion and that that would take it up to about 118.

That has basically been my position. I don't want FHA to compete with the private sector in this regard.

Mr. WYLIE. It could be my question is a little premature and that Congressman Kleczka, who is not here, asked the GAO for a study on this issue.

My time has expired, and we have a vote on. I thank you very much, and I will be back.

Secretary KEMP. I thank you.

Chairman GONZALEZ. The committee will recess for a vote.

[Recess.]

Chairman GONZALEZ. The committee will please come to order.

Ms. Oakar, you were about to be recognized.

Ms. OAKAR. Thank you, Mr. Chairman. Thank you for having this hearing.

Mr. Secretary, thank you for appearing once again. It is always a pleasure to have you before this committee.

Mr. Secretary, I applaud your reforms. I read your legislation, or proposal, I should say. I think it is right on target. But I want to say this for the record, and I wanted to do it publicly because I think it is very, very important to make this point.

The programs were not the reason that there was abuse and fraud and criminal activity. It was not the programs in and of themselves. It was the management of the programs and all kinds of other ramifications.

All of the programs were not ill run. Quite honestly, CDBG is an excellent program that does not need new regulations, in my judgment.

It was the discretionary use of CDBG in the inspector general's report that showed that a couple of favors were given to a couple of Members of Congress in terms of swimming pools and all that.

In and of itself, that program operates very well. So to put up tight regulations that somehow close the gap and don't allow cities options, to me, would be unnecessary. You have to be a little careful about that. I just want to say that.

I also want to point out to you that I am very dismayed. I have to tell you this for the record. I am dismayed that somehow I get the impression that if I call HUD, and it is certainly not in terms of your immediate staff, they have been terrific, but I don't want to feel guilty representing my constituents.

If I think some people on your staff are off base in terms of how they are evaluating certain things affecting my home town—I have to tell you something—I am not going to take it. I think that I am elected to represent the people that sent me here.

One of our charges is to be an ombudsman for our area. If we are not ombudsmen for our area, we have got to be thrown out of office.

On the other hand, if we are asking for something unreasonable or unethical, then that is a whole different story. But if I feel that there is a situation where I am trying to get housing for our area, whatever it happens to be, and I have to feel that I cannot even ask a question. I've got to tell you, I think that is outrageous.

Now, there is such a thing as overkill. Reforms are no substitute for policy. I think you have to do both. You have to have the reforms. That is part of the past, and I'm all for them. I'll be the first one to support your package.

But I also think you have to have a program. You have to get on with the show and tell us what it is you're going to do relative to your being Secretary.

You inherited a terrible situation, and you were ready, I think, to go at new ideas. I know you have them. But I'm anxious to pass on some plans that you have along with my chairman's and this committee's philosophy. You know, I just wanted to say there is such a thing as overkill.

And what you might be doing inadvertently is prohibiting programs that operate well. For those areas of the country that operate their programs with integrity and have seen the effectiveness of HUD programs—you know—we really need those programs.

To me, the purpose of HUD is certainly poverty, but it is also, in addition, a department to create jobs and to demonstrate the ability of our country to provide safe and decent housing and accessibility to safe and decent housing for every American.

I don't mean to do this public little lecture here, but I'll tell you something. I think that there are times when I get the impression that what we are going to do is have this fortress now build up as an overreaction and a substitute for programming.

I for one have to say publicly that I don't want to see that happen. I don't think you want to see that happen. But I want to caution you that it gives me the idea that somehow that is going to happen.

We need a program, and we also need people on your staff. I know you don't have all your staff yet. I think it is outrageous that you don't have them all approved by the Senate.

But I think you need a staff that is sensitive, that when a legitimate question is asked, that they respond courteously and give you really in-depth answers.

If that doesn't happen, I'm telling you, I think that is wrong.

Mr. WYLIE. I think the gentlelady is making an important statement. The implication I don't think has been made by the present people at HUD. But the implication is that, if a Congressman calls about a project in his district, that there is something wrong. I think it is most unfortunate that there have been some statements made like that.

I am sure that the former Member of Congress here, our good colleague, Mr. Kemp, doesn't feel that that it is wrong for us to call about a project in our district necessarily.

Ms. OAKAR. I just want to say, though, also, that I think these regulations that would prohibit well-operated programs in areas across this country would be wrong to change and to stifle the certain degree of flexibility that CDBG has. That would be absolutely outrageous to me because I am not responsible because somebody in New York got a swimming pool or something.

My city operates that program well, and I don't want to see some guidelines change that is going to inhibit my city's opportunity to use its money. Thank you, Mr. Chairman.

Chairman GONZALEZ. The time of the gentlelady has expired.

Mr. Secretary, you have got to leave?

Secretary KEMP. There is an impression being left that I would like to at least, with brevity, answer her—

Chairman GONZALEZ. Well, you have total control of that. you are the one that has to leave. I am just trying to respect your wishes. We would love to keep you here.

Secretary KEMP. I want to assure the chairman and Members on both sides, I am not here with an arrogant attitude. If any man or woman at HUD who is politically appointed or careered at HUD is disrespectful to a Member of Congress, I would personally fire him or her. I am not disrespectful. You have never been treated by me or any of my staff disrespectfully.

We have nothing but admiration having served in the Congress. That wasn't what you suggested. Let me at least put that to rest.

Mary Rose, you are a vital Member of the House of Representatives and the committee that has oversight and has cosponsored legislation with me in the past. Let me say to you I think it is going to be hard for me to defend, and frankly, I think it is hard for my friends on the Democratic side to defend a program that allows moneys to be spent without some guidelines that target them toward fighting poverty, distressed communities, developing those infrastructures that are critical to the development.

But how can targeting CDBG 75 percent to anti-poverty criteria possibly be tightening the program so restrictively that it is not going to meet the needs for which it was designed?

I want to assure the gentlelady from ohio CDBG can work and continue to work. It meets many important goals. I support CDBG. I fought for adequate funding of CDBG. I am not out to gut it. And I don't make swimming pools the sole criteria by which I made my judgment to try to tighten it up to fight poverty.

Ms. OAKAR. That was one instance, Mr. Secretary. If I could just respond? You know, I think that if you look across the country, that is one program that really has been operated in a very comprehensively fine fashion. At least I can say that about my own city. And some of us were with that program from the beginning. We changed the regulations, did we not, Mr. Chairman, to target more poverty targeting for CDBG, and some people didn't like it.

We changed it, and it has operated well. I am saying there have been tremendous abuses. But don't blame the program. We just need better management. We have that management.

Secretary KEMP. You did not hear me blame CDBG. I am a supporter of CDBG. I think it should be targeted about 75, and you think it should be 60. That is hardly Kemp-scorched earth policy in the city of Cleveland or any other place. But I don't think our argument is as divisive as it might appear.

You have my assurance on both sides of the aisle. If anybody calls us, you have a right; you should be fighting for your city. If you want a rock and roll museum built in Cleveland and you think that is a legitimate use of UDAG funds and we study it and say but for UDAG it could be done in the private sector, that is a legitimate argument.

If anybody treats you with disdain, they will be fired.

Ms. OAKAR. If I want housing in downtown Cleveland and I found some phony boloney relations put up as a smoke screen so

our area does not get housing for downtown Cleveland, you better believe I am going to fight that.

Secretary KEMP. Good. I am a fighter. I sent my Under Secretary to Cleveland. I plan to go to Cleveland. I want to be a successful HUD Secretary.

I can't do it without your help, but I have to call them as I seem them. We don't think a UDAG grant for a rock and roll museum necessarily fit the criteria. It did not fit the criteria. If I don't have criteria, you are going to haul me up before this committee and have my head for doing things that are not fighting poverty, building houses, taking care of the poor and meeting the criteria that have been laid on me by the U.S. Congress with which I agree.

Ms. OAKAR. Just for the record, I was not necessarily talking about that grant, Jack. I frankly am a little dismayed you raised that. If you want to debate it, I will be happy to debate it publicly with you.

Secretary KEMP. I don't want to take on rock and roll.

Mr. ROTH. Mr. Chairman, I think it is inappropriate to say the people are the problem, not the program. That is going a little bit too far. I think the programs are the problem.

Secretary KEMP. There are flaws in the programs. I didn't blame all the programs. I didn't say it was systematic. It would have been easy to do because there are some really flawed programs.

Mr. ROTH. My opinion is you didn't go enough in that direction. I think the problem does lie with the programs to a great degree. To make Members of Congress feel good by saying, these programs aren't the problem is a bunch of baloney.

These programs must be cleaned up. The Secretary of HUD has to be like a quarterback on a football team. If the fans were going to call the plays, you won't call any plays. We have to have a quarterback in there, Mr. Secretary, and you are our quarterback.

That is why I think we have to take some direction from you. These programs are flawed. That isn't to say we are going to change a few people who are not going to get the job done.

Secretary KEMP. I beg of you not to use football in metaphors, but since you used them—

Chairman GONZALEZ. The Chair will recognize Mrs. Roukema. She had been seeking recognition, and I didn't notice her. I was going to say at the very outset I said it was more a people's problem than a program problem. We are seeing things in very diametrically opposed ways.

Secretary KEMP. There is plenty of blame to go around. There was gross mismanagement of the programs. There were some systematic flaws we are trying to correct. I don't think it makes for rational discourse to try to say it was all one or the other. We are going to put an end to it.

Instead of cursing the darkness, let's light some candles. The gentlelady from New Jersey is one of the chief candle-lighters for reform, and I would like to hear her question.

Mrs. ROUKEMA. Thank you, Mr. Chairman. Do you have time for just another few minutes.

Secretary KEMP. I do.

Mrs. ROUKEMA. Let me ask two quick questions. If you cannot give me an answer now because they obviously in one case require

more time, otherwise you would have included it in your statement.

I will start in the reverse order. But I would like to follow very closely what you have been saying on page 11 concerning the layering of HUD's subsidies. I think this gets to the heart of a very important issue. It is to the issue of where some programs are absolutely wrong.

That is a structural problem right there. In addition, there were abuses of even the structural problem. The abuses that were attendant to this are mind-boggling in terms of the actual fees. But you have not given any specifics here, so I assume that you don't have the specific legislation as to how you are going to precisely prevent the double-dipping that you have referred to and also reforms in the tax, the syndication and the tax benefits.

That is on page 11. So I would like to be working with you. I think every member of this committee would like to bird-dog this issue. You may have the final version actually ready or close to being ready. But do you want to amplify on this beyond what is stated here?

Secretary KEMP. First of all, I appreciate the question. The legislation we are going to send to the Hill specifically addresses the question of double-dipping by allowing us to adjust our subsidy to the level of the tax benefit that the syndicator or syndication receives from the LITC.

Mrs. ROUKEMA. You would no longer have the most egregious examples where people get \$1,500 per unit in consulting fees and then the multiplicity of the syndication of tax subsidies amounted to mind-boggling profits?

Secretary KEMP. Absolutely.

Mrs. ROUKEMA. Hundreds of millions of, if not billions of dollars in some cases.

Secretary KEMP. Yes, Mrs. Roukema. You are going to have that quite soon?

Secretary KEMP. By regulation we are going to require that—

Mrs. ROUKEMA. By regulation are you doing this, not legislation?

Secretary KEMP. I understand I can do it by regulation, that we can count up the value of the subsidy, the tax credit and the value of the syndicated tax credit and then adjust our subsidy under section 8 to make sure that there are no windfall profits.

I am not opposed to windfall profits in private enterprise, but I am opposed to them when people get new Government programs. We are going to put an end to those outrageous fees and profits and conditions that are programmatically flawed, for the record.

Mrs. ROUKEMA. We will look at the record and see if we feel there is a need for legislation beyond that. I appreciate your leadership there.

The second question I have regards a certain dead end that I reached when I was trying to make crimes out of some of the egregious activities that we saw going on at HUD. One you referred to, for example, was in the Robin HUD property disposition situation.

Of course, the person that benefited, the so-called Robin HUD, may be under considerable indictment. My concern is about the people in the Department. It would seem that the people in the Department who aided and abetted are not considerably liable. I

would like to know whether, sir, you and your staff think they should be.

I would like them to be, quite frankly, but I have not been able to figure out a way that you do that in terms of writing the new legislation.

Secretary KEMP. We were just kind of discussing as you were asking the question.

Mrs. ROUKEMA. It is a troublesome question.

Secretary KEMP. I don't think anyone at HUD was handing out the information. If they were, that is a considerable violation.

Mrs. ROUKEMA. Under present law, if the people at, staff personnel—

Secretary KEMP. Well, General Counsel Frank Keating, I am going to ask him to elaborate. I want to make sure I am on the record with regard to Robin HUD. She is no Robin HUD. She was not stealing from the rich and helping the poor. She was stealing from the poor to enrich herself. So she should not be considered a Robin HUD.

Chairman GONZALEZ. Why don't we go ahead and excuse the Secretary. You stayed over 15 minutes beyond the time you said you had to leave.

Secretary KEMP. I will be happy to come back. I appreciate the forbearance.

Chairman GONZALEZ. I think in all fairness to you, we should release you and allow you to leave.

If Mr. Keating can stay, as he indicated, we can have those answers. Whatever else we have, we will submit in writing.

Secretary KEMP. Thank you.

Mrs. ROUKEMA. Mr. Keating, please. Thank you.

Mr. KEATING. Mrs. Roukema, the violation that you referred to involving the Robin HUD matter, all of those allegations are currently covered under Federal criminal statutes, everything that has surfaced to date. In the event a HUD employee giving information to an outsider in advance of public disclosure for money, that presently is covered under our bribery statutes.

In the event that a HUD employee, whether or not he gives information for money or not, gives confidential U.S. Government documents, witness the ill-wind situation at the Pentagon. Insider information at HUD; that is, in effect theft of Government property. That is covered by criminal statutes. What Secretary Kemp seeks is another layer, if you will, on top of that to give him the authority to apply civil penalties up to \$10,000 per violation, even upwards of \$1 million.

Mrs. ROUKEMA. In what kind of circumstances? Could you be specific?

Mr. KEATING. In a circumstance where any of the HUD programs, that is the regulations or the statutes are violated, but without any existing criminal statute to cover it.

For example, at the present time we have really two extremes, we have the ability to, in effect, outlaw conduct under the criminal statutes, prosecute somebody or, as in the case of the co-insurance program, take somebody out of the program by limited denial of participation, but that huge chasm in the middle, that middle ground we don't have the kind of tools that Secretary Kemp needs

to rap knuckles with civil penalties, as is the case in many other departments and agencies of the Government.

Mrs. ROUKEMA. Are you saying that the legislation you have proposed would cover those instances with civil penalties?

Mr. KEATING. That is correct. The package the Secretary sent to OMB yesterday did cover all of the conduct that I believe that your are concerned about with criminal penalties.

Our point is the existing criminal statutes would cover the other conduct with criminal penalties.

Mrs. ROUKEMA. Thank you. That is very helpful.

I would like to yield to my colleague from Massachusetts.

Mr. KENNEDY. Just briefly. Given the criminal penalties that you have just mentioned, why aren't some of the higher up people at HUD in the previous administration being prosecuted under those statutes?

Mr. KEATING. Mr. Kennedy, I can say as a former U.S. attorney it takes a long time sometimes for criminal cases to be put together.

All of the information that Mr. Adams presented to Secretary Kemp, all of the allegations of misconduct, wrongdoing, program abuse that were presented to Secretary Kemp after our review for the purpose of implementing a comprehensive reform package, that information was given to the Justice Department immediately to the appropriate officials at the Justice Department for the purpose of review for criminal prosecution if warranted, and that is their—

Mrs. ROUKEMA. If the gentleman would yield.

Mr. KENNEDY. Sure.

Mrs. ROUKEMA. There is some question about whether Justice has been moving aggressively enough. There are many who feel that they have been, that they are being prudent in terms of their investigation.

There are others who feel that there may be a need for a special prosecutor, but there is no dispute about the fact that they are under criminal liability.

Mr. KEATING. Yes, the Public Integrity Section of the Justice Department is, I think, one of the very credible groups at Justice, and they have all this material at this time.

In our view, and Secretary Kemp has said as much in the recent past, in our view the Justice Department is moving properly and appropriately to review the allegations and to determine if, in fact, criminal prosecution is warranted.

Mr. KENNEDY. I thought that in the newspaper there were indications saying that the Justice Department didn't feel there were criminal prosecutions that were going to come out of this scandal.

Mrs. ROUKEMA. Maybe Mr. Keating could answer that.

Is the gentleman from Massachusetts correct that Justice has disavowed any question of—I thought it was still under review?

Mr. KEATING. I think Congressman Kennedy is correct as to the original materials that were provided. There was a decision, at least apparently made public casually or officially or otherwise, I don't know, that there was not enough to warrant criminal prosecution at that time, but as the Member is well aware, there are other facts that are being developed.

I know a number of committees are examining allegations——

Mr. KENNEDY. But, Mr. Keating, if you are a former attorney, then it doesn't seem to me you are going to stand in the way of a bunch of bureaucratic gobbledygook if there are people who have violated the laws, have taken money from HUD, have taken taxpayers money and abused it.

Going through the exact same statute you just went through in answer to Mrs. Roukema's questions, you indicate that you are going to be able to prosecute people like—or anybody that was dealing inside information at HUD.

Now, it seems to me, if you have people who are much higher up than the people Mrs. Roukema was talking about who are, in fact, doing that, then if you are a former U.S. attorney, simply because you are sending it over to the Department of Justice and finding that they are doing the slowdown on it, it seems to me you have an obligation to this committee to indicate specifically what is going on with these particular individuals and whether or not prosecutions are going to be moving forward.

Let's not hand it over to the Department of Justice, if they are putting out press releases saying that they don't feel they have enough information to go after the individuals.

Mr. KEATING. Mr. Kennedy, I don't think it is fair to describe any referral to the Justice Department of all of the facts developed by the inspector general as bureaucratic gobbledygook. That happens to be——

Mr. KENNEDY. You just reviewed with me the fact that you have read in the newspaper as well as I have read in the newspaper that they don't feel they have the muscle to move forward on those prosecutions.

You have also sat here and told us about how these abuses have taken place, and it did seem to me that the natural process is you can say whether it is bureaucratic gobbledygook or not, the point is whether or not these individuals are going to be prosecuted. It seems to me you have an obligation as the chief law enforcement officer at HUD to make darn well certain that the people that were abusing this system at HUD are going to be prosecuted, and don't tell me you have just sent it over to DOJ. That is your responsibility, not the Department of Justice. That is your responsibility, and it is this committee's responsibility to make sure you do your job.

Mr. KEATING. It is not my responsibility. Let me explain.

Mr. KENNEDY. Well, it certainly should be.

Mr. KEATING. The reality is that all the information that the inspector general developed, all of the information we reviewed, all of the information that suggested program abuse, misconduct, and incompetency is addressed in the Secretary's comprehensive reform package, legislative, regulatory, administrative.

Those facts which could suggest, suggest the authority for criminal prosecution, and there were very few of them at the time the inspector general's reports were developed and given to us, were referred to the Public Integrity Section of the Department of Justice for further review and action. They make the decision.

The grand jury will determine whether or not prosecution is in order, the Justice Department determines whether or not prosecution is justified. What we do, as responsible to this committee, is to

clean up the mess at HUD, not to prosecute anybody, and we are in the process of doing precisely the former.

Mr. KENNEDY. Well, it seems to me—I will revert back, but it seems to me you have a distinct responsibility as the chief law enforcement at that agency to make darn well certain that the people that you are working with that are abusing that agency and abusing the taxpayers trust are, in fact, going to be prosecuted, and to slough it off to some other agency and say it is their job I think is an outrage.

Mr. KEATING. We are not sloughing it off to anybody.

Mr. KENNEDY. It sounds to me like you are

Mr. KEATING. We will continue to work with them to make sure justice is done.

Mr. KENNEDY. We will stay on top of that.

Mrs. ROUKEMA. Reclaiming my time, I think I understand what Mr. Keating has said, and I understand what my colleague is saying here, the only reservation I have, I am not a standing member of the Oversight Committee that is investigating this issue, nor am I a member of the Judiciary, but it is my understanding that Mr. Lantos never questioned the role of the Justice Department here and that it was their jurisdiction and absent that, then they might pursue the question of a special prosecutor.

Mr. Frank may know more about that than I.

But thank you, Mr. Keating.

I appreciate your information.

Chairman GONZALEZ. I think in all fairness, though, to the witness, when did you become counsel, Mr. Keating?

Mr. KEATING. I became over, roughly, March 1 and was confirmed in June.

Chairman GONZALEZ. This year?

Mr. KEATING. Yes, that is correct.

Chairman GONZALEZ. Well, I didn't want the inference, and I think without meaning that Mr. Kennedy may have raised an inference to parties not having a chance to follow the course of events too carefully that you were on board at the time the occurrences referred to took place, and I wanted to make sure the record showed you weren't, that you are on board now with a no charge, as you say, as of March or June.

Also, the fact is that Mr. Lantos was quoted over the weekend and as saying that he was positive that people would be going to jail.

Now, what the basis of that statement was I can't tell you. I haven't seen the newspaper story that Mr. Kennedy alludes to, and not having that knowledge, I don't know what the Justice Department is referring to precisely as to what they don't think is subject to prosecution.

However, our experience with this committee and the subcommittee on Housing in the past has been that in the course of gathering testimony here and elsewhere, such as Milwaukee, Chicago, Flint, MI, we did adduce testimony indicating some criminal culpability.

We then at that point referred to the inspector general. HUD had not had an inspector general since its inception. That was something that grew later. Before that we had hearings in the

Small Business Committee, and we came across new testimony that showed a criminal culpability, we made a direct referral to the Justice Department. Mr. Keating is correct, Mr. Kennedy, there is nothing he can do about prosecuting.

He has to refer—I know what you mean by following through, but given the hierarchical definition of jurisdiction, even if Mr. Keating felt that people should be prosecuted, that decisions rests exclusively over in the Justice Department.

Mr. KENNEDY. Well, Mr. Chairman, I could begin to disagree to some extent, I think that it is fine that there is a bureaucratic system in place that the prosecutions are handled by the Department of Justice, but nevertheless if Mr. Keating is aware of individuals that have blown the law at HUD and sees that there is another Federal agency that is not doing its job, after all, this is a political scandal.

It is a scandal that was done by an administration, and that administration also appoints the individuals in charge of making these decisions at the Department of Justice, and for us to sit as the authorizing committee, to sit back and let an internal governmental process take place without oversight by elected officials that have a direct responsibility to the individuals in this country that have vote for us and don't vote for us, it seems to me we are abandoning our responsibility.

What I am trying to suggest is—and I didn't mean to imply that Mr. Keating was there at the time the abuses took place. I don't think that is really relevant. I do think that it is relevant that this was a scandal that took place by the individuals involved in that administration, involved in the administration at HUD that we have a responsibility. Everybody is here today talking about the reforms that HUD is going to make, but the essential reforms could have been made and could have been done without any involvement of this committee.

These are essential regulations that are going to be changed at HUD, and it involves an essential trust between the executive branch and the legislative branch, and that trust has been broken. What I am trying to suggest, sir, is that it is incumbent upon the individuals at HUD if one branch of this Government is going to trust the other, to make certain that those prosecutions are, in fact, followed.

Mr. WYLIE. Could I ask whose time are we on? The gentleman has made an excellent political statement, and I think we know where he stands on the issue.

Chairman GONZALEZ. Well, actually I yielded to Mr. Kennedy. I have the time. I took the time, and the reason was to clarify and make sure that no witness answering our summons would be in any way placed under a cloud. Unintentionally or not, that wasn't fair.

Mr. VENTO. Mr. Chairman——

Chairman GONZALEZ. Just a minute. I think, Mr. Kennedy, with all due respect, I know where you are coming from. I share your sentiments. Even before you came on board I had been quite cast in the role of an opponent to the then Secretary of HUD, but we nevertheless persisted and we did have oversight.

In fact, you are involved now in what would be considered oversight responsibilities so that no matter how much we would want to, though, we have to exist and co-exist within the limitations of the constitution, and the legislative branch is coequal, separate and independent, but nevertheless not superior to the executive branch, and the executive branch is that branch under the constitution that is charged with faithfully executing the laws, and that implies implementing the criminal statutes and prosecuting those culpable of transgressions.

But I think that in your enthusiasm you have confused the proper jurisdiction and the limits attached thereto. We may think that we know that all of this that is now being publicized happened during a past administration, but I think the inference would be wrong if we were to say that—I have always said that corruption is bipartisan.

Every time a particular partisan approach was used either by those in or out of power, alleging the wrongdoing of the opposite party, whether it was in power or not, usually when it was in power because those seeking power will use that. It turns out that once in power, the same thing happened with that administration.

I think the best illustration goes back to the time of President Truman and President Eisenhower. Truman, you will remember—no, you weren't born then. But Truman had his assistant—I forgot his name—Donovan or somebody—and he was accused of 5 percent, selling influence at 5 percent. Eisenhower came into power and pretty soon you had Sherman Adams at 15 percent, so that corruption is bipartisan, and what we have here now is a new administration. Yes, Mr. Kemp was part of this body at a time when all of this was going on.

He wasn't a member of this committee. Yes, it was the other party that was in power, but I think that we have to keep always limpidly clear what the correct constitutional grant of power is inherent in each one of these organs of our Government. I think for you to say that unless Mr. Keating personally prosecutes or implies that that somehow or other he is in default is quite unfair because that is—

Mr. VENTO. Mr. Chairman?

Mr. FRANK. If the chairman will yield?

Chairman GONZALEZ. I will give rebuttal time to Mr. Kennedy.

Mr. KENNEDY. I won't take much rebuttal time. I will just say I disagree with you, Mr. Chairman.

Mr. VENTO. Mr. Chairman, I don't know where we are in the questioning process, but I think that what Mr. Kennedy is concerned about is a concern that we all have, and that is that here we are with a whole package of new law, new administrative change, and what we are concerned about is enforcing the existing laws, and we find in many of these instances that there were laws, there were rules, and we want to see the diligent execution of those existing laws.

These funds had programs and limits in them, but I think that that is imperative before we go off and rewrite the law, we ought to know what is wrong with the ones that we do have, and I think there is a tendency here to say, well, the law is deficient, and

therefore we are going to take care of this by passing more laws, and I think that that, Mr. Chairman, is not appropriate.

I think we—I think that is really what we are all concerned about. I don't care if they are Democrats or Republicans, I don't think Mr. Kennedy interjected that. He said there were problems; he wanted to see them resolved. Passing them to the Justice Department—Mr. Chairman, you well remember my little episode in the last administration with an improperly awarded UDAG grant.

They passed that over to the Justice Department, the Justice Department finally recovered the money. I wasn't very happy about it. I know the chairman and others assisted me in this committee in that process, and finally we were able to prevail—but it isn't easy for us to do it.

Somebody said Congress discovered these problems, I think we are still in the discovery stage—

Mr. BARTLETT. Mr. Chairman—

Mr. VENTO. I think I am under my time, Mr. Chairman.

Chairman GONZALEZ. Yes, Mr. Vento, is still within his time.

Mr. VENTO. I had planned to make another comment. I think the fact is we are still in the discovery process. We are still in the prosecution process at the Justice Department with regards to these issues. Congress did do its job and has in the past. But it is not an easy or simple task, and I think that to run in here and say we are going to change all of these laws now because somehow they are deficient is not necessarily correct, and we really haven't understood the magnitude of what has happened.

Finally, I might repeat again what I said in my earlier comments. We don't know what the policies are that we are going to be trying to administer, so trying to improve now would be a static method in terms of whatever new policies we develop in housing, so I think these must go through.

I commend the Secretary and the staff for what they have done. I think that they should do administratively what they can, but we do have these two other problems with new policy changes that are not in place that are likely to be approached.

The second problem is prosecuting the law, and the third of course, if I can add a third problem, we have to find out what the magnitude of this problem is. We are not done until we have concluded that, and our colleague, Mr. Lantos, and others on the other committee and to some extent our own, have been involved in plumbing the depths of that.

Unfortunately, the news has not been very good. I know that you have sought and received some changes in other areas. I would yield to the gentleman from Massachusetts if he had any—I know he was seeking recognition a moment ago.

Chairman GONZALEZ. The Chair intends to recognize him in his own right.

Mr. VENTO. Well, Mr. Chairman, he has been waiting, and others were here before me, so I won't proceed with questions at this time.

Chairman GONZALEZ. You have about half a minute. But I was going to ask you to yield.

Mr. VENTO. I would yield to you, Mr. Chairman.

Chairman GONZALEZ. I would like to say there is no disagreement. In the first place we don't have in bill form the Secretary's

proposals yet, so we don't know exactly what legislative recommendations we have until we see the particulars of the bill.

We hope before the day is out we will have it. Mr. Wylie and I—

Mr. VENTO. Mr. Chairman, what is the date today? Is today October 13? The 12th? Twelfth, Columbus Day. We are planning about another month and a half of session, Mr. Chairman?

Chairman GONZALEZ. I don't know.

I don't know that anybody knows how long we will be in before we adjourn sine die or rather adjourn for this session. I would say, though, that until we have that bill, we won't know what specifically the Secretary is asking us by way of legislation.

We in the meanwhile are not going to stop the further consideration of our reauthorization package, which is ready for markup. Mr. Bartlett?

Mr. BARTLETT. Thank you, Mr. Chairman.

Mr. Chairman, I do issue my apologies to the gentleman from Minnesota. I had completely lost track of who had the time, and I apologize for interrupting him a moment ago.

Mr. VENTO. I understand.

Mr. BARTLETT. I didn't realize he was at that point on his time. I want to say to both the Deputy Secretary and general counsel, I think this is a positive day.

I am generally supportive, as I think most of the committee is, of the legislation you are proposing to reform the processes at HUD. I am impressed by the introduction of sunshine and accountability at HUD, by the elimination of some, and I would hope at some point would be of all discretionary funds and change all discretionary funds back to formula grants by the introduction of some rather severe official management proposals that are long overdue at HUD, and by targeting low and moderate income families with CDBG money and with other HUD proposals.

I do have some specific questions on the legislation. First, as I read your legislation, I see that I believe that you are seeking to overturn what is my understanding was a court case called the *Rainier View* court case, and thus your legislation would seek to require only a market analysis of rents of several of the project-based assistance that were granted some 15 years ago or so and stop comparability analysis.

First, can you tell us, is that your intent in this legislation and if so, would you give us your reasons for that.

Mr. KEATING. Mr. Bartlett, if I could attempt to take that briefly for you, we are not attempting to overrule a court case per se. The litigants in that court case, the plaintiffs have been paid. What we are attempting to do is to stop the hemorrhaging that will cost the taxpayers upwards of a billion and a half dollars over the course of the next 10 years for the payment of what we see as windfall payments in excess of what fair market rents, including comparability should be.

The *Rainier View* case that you refer to was a Ninth Circuit Court of Appeals case in California in which the court decided that HUD was wrong in the way we were setting our fair market rents in attempting to factor in comparability, that is what does the market will bear in that particular area.

We believe we should be able to factor in comparability because to pay people 120 percent of market plus more on top of that is an excessive windfall. It is inappropriate, as Secretary Kemp said when he was explaining his concern about this issue. It takes from low and moderate income Americans who form the traditional needs of HUD a large body of cash.

We think to pay the decision in the ninth circuit could cost us as much as \$300 million. To pay it across the United States could cost us up to \$600 million or a billion. We are not sure. At this time we do need help from the Congress, because we think to pay people a fair rent to provide for low and moderate income is one thing, but to pay people an excess rent, to pay people a windfall is inappropriate.

Mr. BARTLETT. So your legislation would change existing law to provide for only market analysis and not for comparability of standards, that's your proposal?

Mr. KEATING. Well, we are attempting to clarify the law to permit comparability to be a factor, that's correct, Mr. Bartlett.

Mr. BARTLETT. Would you intend for that to be retroactive or effective on the date of enactment from this day forward or would you use the comparability and market analysis for prior—for retroactive?

Mr. KEATING. Mr. Bartlett, that of course, would be up to this committee and the Congress. We would hope that it would be retroactive.

Mr. BARTLETT. So your proposal is to make it retroactive back to what date?

Mr. KEATING. I am not sure what the day is, Mr. Bartlett. It would probably be from the date of the decision prospectively.

Mr. BARTLETT. From the date of *Ranier View*?

Mr. KEATING. Yes, but I am not exactly positive what that particular threshold is.

Mr. BARTLETT. I may caution you. You may have some difficulty. I would hope you would have some difficulty with Congress in adopting a retroactive application of the law. Obviously, we will look at it when it comes up here. Third, you are telling us you are not certain what the costs would be. I have seen three or four different estimates, somewhere between \$200 billion and your highest estimate this morning was \$1½ billion.

When will you have a handle on what these costs will be?

Mr. KEATING. The best estimates we have, and I was speaking just a minute ago with Mr. Edson whom I know represents a number of the plaintiffs who disagrees with the figure, but the best estimate we have is the \$130 to \$150 million within the ninth circuit, upwards of \$600 to \$900 million throughout the United States retroactively, and then prospectively upwards of \$1½ billion.

Mr. BARTLETT. OK. The next question is you proposed the elimination of discretionary programs of some types in this legislation. I want to pin that down for a minute. Are you proposing—the only specifics I see, but it may be more. Are you proposing the elimination of those accounts that are known as the Secretary's discretionary funds or are you—would you propose the elimination of discretionary projects in general and a movement of HUD funding over to a formula grant?

Mr. DELLIBOVI. Mr. Bartlett, we want to do two things. We want to eliminate the discretionary fund itself, but in the other programs, the housing programs, we want to eliminate the headquarters reserve which was used as a discretionary fund for discretionary purposes.

We believe that the money and the benefits should be allocated on a fair share formula basis to the localities or on the basis of competition. There may be a need for special initiatives. We had one operation boot strap that the Secretary proposed, which was a new initiative that he proposed.

We want to have clear criteria laid out, laid out before the funds are set aside at the beginning of the fiscal year so that everyone knows what the rules of the game are, how they are going to be played, and what the rating and ranking system is going to be.

Mr. BARTLETT. So you would leave some discretionary funding in the HUD program, but you would try to limit it and you would make it—let me see if I understand. You would convert it to an open competition announced at the beginning of the year. The reason for my question is much of the controversy came from the mod rehab programs which we are purported to have been competitively bid, but we come to find out the competition was—

Mr. DELLIBOVI. There was no competition in mod rehab. I think the facts speak for themselves, although we have now heard people say that there was a competitive process. We have found not a scintilla of evidence that there was any competition in the way those funds were awarded.

Mr. BARTLETT. So would you propose to either, A, eliminate mod rehab, which frankly I think would be a good idea?

Mr. DELLIBOVI. We have proposed the termination of the mod rehab program. It was discredited. It didn't work. Even where it was used it wasn't efficient. We believe its time has come and gone.

Mr. BARTLETT. So you would propose to eliminate mod rehab?

Mr. DELLIBOVI. We do.

Mr. BARTLETT. And to eliminate all the discretionary funds you can, and the ones you can't, then in your proposal you would propose to set it up on a competitive process, the competitive rules are set at the beginning of the year and not engineered for each individual grant?

Mr. DELLIBOVI. That's correct, Mr. Bartlett, and those competitive situations would be the exception rather than the rule. The general rule is going to be to fair share it with a formula. There are certain programs which are so small that they just don't work. If we divide all the units to every community in America, a small city may end up with two or three units and they can't do anything with them.

Mr. BARTLETT. Mr. Secretary, it would be helpful to this committee when you submit this legislation, and we could hold the record open, if you could submit to us the list of those exceptions that would continue to be a competitive process and a summary description in lay language as to how you would ensure it would be a competitive process.

Mr. Chairman, if I have time—I don't.

Chairman GONZALEZ. Time of the gentleman has expired.

Mr. DELLIBOVI. We will be pleased to submit that material for the record.

Mr. FRANK. I will get my questions in before we vote. One of the problems we have in dealing with the reforms only and not other substance to me comes up when you talk about one of the reforms you propose is to abolish the mod rehab program.

Is there going to be in the proposal and alternative suggestion of what to do with that money?

Mr. DELLIBOVI. The money that was used for the mod rehab program would be—the certificates would be used for one of the other programs that we believe are working.

Mr. FRANK. But wouldn't you in the reform package have to make that decision? In other words, if as part of the reform package we are terminating a particular program that gets money into low income housing, unless we are prepared to have a gap of some period, we have got to figure a different place to put it, I mean inevitably.

Mr. DELLIBOVI. Well, the funding of the mod rehab program at about \$250 million, there are more than enough initiatives—the Secretary asked for \$50 billion for homeless programs, \$44 million for a new home ownership program.

We did receive that. So we have plenty of recommendations.

Mr. FRANK. I understand that. But you are then agreeing with me as part of the reform package there would be some new authorization. We would have to decide—or are you saying—

Mr. DELLIBOVI. Not necessarily. There are a number of programs that we have already authorized that we could fund.

Mr. FRANK. Would the legislation be silent on that and it would be the Secretary's decision where to put the money?

Mr. DELLIBOVI. It would obviously be the Congress' decision.

Mr. FRANK. That is my point. I am not saying it is a hard decision to make. I am saying it is a decision to make. If we are going to decide not to spend money here, we have to decide to spend it elsewhere. I have a more fundamental question here.

Secretary Kemp has been a great advocate during his political career of the importance of putting the free enterprise system to work. I don't want to lose that. For instance, on page 11 you talk about preventing the layering of subsidies by having people do double-dipping with the low income tax credit, and so forth.

I agree in some cases that has led to abuse. On the other hand, I think a no double-dipping at all move will result in an underusage of it.

Mr. DELLIBOVI. We fully agree, Mr. Frank. We want to have the tax credit available to make the deal happen, but not as the Secretary said to make the windfall profits.

Mr. FRANK. We had the Attorney General in on the Americans with Disabilities Act, and then later on it talks about a redirection back to the poor, the tenants, community-based nonprofits, and so forth.

I am for that, but we don't run any other Department of Government that I am familiar with wholly on a nonprofit basis. Maybe the State Department gives its money to nonprofit entities called other countries, although a couple of them got profitable.

But the Defense Department isn't asked to only deal with non-profits, the Commerce Department isn't, HHA isn't, the drug companies aren't. Part of the problem, I think, we have run into and I think we over did the cutbacks of the tax credit, and I think the Secretary agrees there, even though maybe he doesn't like to agree as much as he did, and I think we did it also with regard to some of these programs, and that may be one of the things that we were talking about the section 8's on fair market rents.

That is we can't order people to invest their money in low income housing. We can't put up all the money out of the Treasury. We need to have incentives that are going to have private sector people put up money, and I just want to make clear that we agree we don't want to overreact to the abuses, and there have been some abuses, by discouraging it.

We can't do it all with nonprofits. We can't do it all with charity. There is a legitimate role for a set of both tax incentives and government matching programs that do provide incentives to the free enterprise system. Some things taken here could have gone the other way. I want to make sure we agree on that.

Mr. DELLIBOVI. Mr. Frank, I want to assure you the Secretary feels there is a legitimate role for the private sector. We believe that that role includes taking some of the risks, and having reasonable profits.

What we are opposed to is the windfall profits.

Mr. FRANK. I think you can separate it out. The consultants seem to me to be very much unnecessary. It came up when we were talking to Mr. Watt. His consultancy fee in that reduced the return of the developer, as she testified, basically from about 11 percent to 8.5 percent on her equity.

The difference between 11 percent return and 8.5 percent return probably gets you out of where it makes sense to do entrepreneurial work and into where you just put your money somewhere.

There is no question about it. Even if the consultant fees are being paid for by the developer, if we reduce the developer's profit by a set of procedures that require him or her to pay a consultant, we may be diminishing people, and I appreciate that.

The last thing I would just reiterate what others have said, the basic problems here were not, it seemed to me, statutory. They were personnel. We should go ahead with some statutes, but I don't think anyone ought to—nothing in the law made people do these things wrong.

They volunteered to do them wrong, particularly, and I have to divide this out, the co-insurance program where it seems to me we lost more money than in mod rehab, yes, there I think it was more statutorily. We should be clear that different programs require different responses.

Thank you.

Mr. DELLIBOVI. I'll just respond on the co-insurance program, I think co-insurance is a program that could have worked very well. One of the problems with that program is that all of the risk was left with the government, and all of the profits were left in the private sector. That is not my idea of privatization. It's not Secretary Kemp's idea.

There should be a sharing of both the risk and the profits.

Chairman GONZALEZ. Once again, I want to thank our distinguished Member from Massachusetts. I think he has hit the nail right on the head with his incisive points.

Now we have three Members that have not had an opportunity to ask questions on their own. Are the witnesses under any time constraints?

Mr. DELLIBOVI. Not particularly.

Chairman GONZALEZ. Would you be able to bear with us if we took a vote and came back?

Would you prefer that, Mr. Carper?

Mr. KENNEDY. I can submit my question in writing.

Chairman GONZALEZ. Well, I have some because the main purpose for these hearings today, I felt, would be to show the evidentiary need for program restructuring or abolition of the program.

Up to now, I have had very little, because in the case of section 8 moderate rehab, I know what the intent was on the part of the Congress. But with the advent of the Reagan administration, we had a departure from the method allocated.

For instance, you have seldom had more than 20 units. It wasn't until these later days that you had 300 very, very antithetical in nature to what the congressional intent was.

So I would like to come back and have some testimony so that we can back up as much as possible the legislative recommendations.

We will go take a vote.

[Recess.]

Chairman GONZALEZ. The committee will proceed, and again, thank the two witnesses for being patient and being with us and going through the lunch period.

Mr. Carper.

Mr. CARPER. Thank you, Mr. Chairman, and again to our witnesses, thank you for sticking with us.

A couple of questions I would like to cover. In reviewing a hand-out that's entitled Reform of HUD, I have read through it fairly carefully.

In our side bar conversation, you have indicated that this package really looks retrospectively, it looks at the past, it looks at the problems that you have inherited and are endeavoring to try to clean up, in some cases with our assistance.

One of the problems that we did not resolve earlier this year is the issue of preservation. We have essentially punted. We have put off until next February the day of decision on how to ensure that in some cases hundreds of thousands of people who are in units around the country, how they might not end up out on the street.

We are going to be faced again in the next couple of weeks, maybe next 2 months, 3 months what to do about this issue.

I don't want us to have to punt again. I want us to work out a compromise, something you folks are happy with or satisfied with.

I am wondering if you could give us today your benefit of your thinking on the issue of preservation and what we do now and between February 2 on what to do and not to side step.

Mr. DELLIBOVI. Mr. Carper, Secretary Kemp sees the effort in two parts. That which we are discussing here today he refers to as clearing the decks, and that is exactly what we wish to do is to clear the decks so we can then look prospectively at a new authori-

zation and dealing with problems such as the prepayment, the preservation issue.

As you know, the Congress has placed severe requirements on mortgage prepayments. Those restrictions go to February 1990. We are developing proposals that we believe will protect the tenants and the rights of the owners, and we want to work with the Congress when we present them very shortly.

We hope that we will be able to come up with a set of proposals for your consideration that will enable a resolution of this issue before the February deadline is reached, but in the event that we do not, we may need a brief extension.

However, it is our intention to resolve this issue.

Mr. CARPER. I have encouraged the chairman of our full committee to bring an authorization bill that would include the reforms that you folks have outlined, to bring that before a subcommittee mark up by the end of this month.

I further encouraged him to bring the bill before the full Banking Committee by the end of November in the hopes that we would have a housing bill on the floor once we come back in, late January, early February.

I think it's important that the prepayment issue be addressed. Again, I would urge you to move with all due speed. I know you have inherited a can of worms, you have your hands full, you're trying to deal with these issues. But this is another important issue that is facing us.

Again, we put it off once. I don't want us to do that again. I would just say to the extent you can divert some of your attention to this, please do.

The second issue—

Mr. DELLIBOVI. Mr. Carper, if I may just respond to that. We are very concerned about moving a reform package, clearing the decks. We understand the need to deal with preservation. We understand that next year there is a need to deal with the reauthorization.

You are correct in pointing out that we have inherited a can of worms, and it is absolutely necessary that we stop those worms from eating the fruit of the HUD programs and destroying the programs underway.

We believe that reform needs to be passed as soon as possible so that we can clear the decks and deliver the programs that we now have authorized and are underway. It would be a tragedy if our effort to clean up HUD is derailed while we wait for the legislative process, which is not always the fastest process. I say that with all due respect.

I was a State legislator in New York State. I understand that there are two houses in this process, and it's a very complicated process, and I would hate to see our reform effort—our effort to stop the Robin HUDs, our effort to stop the rip-offs—derailed while we wait for some new authorization of an expensive program that is yet to be developed.

I noted that in the other house just last week the majority announced a whole new task force to figure out what they want to do about a reauthorization, and that is their right if that is the way they approach it. But we cannot wait. We cannot delay cleaning up

the programs that now exist while we wait for the new task force report.

Mr. CARPER. We, I think, in the Congress have waited patiently while Mr. Kemp put together his team, and I think it's a good team. We have waited patiently. We have waited for you folks to develop your legislative initiatives.

Now that we are receiving those, we have been literally holding off, I think, the markup of our housing bill in anticipation of your input. We are now beginning to receive that input.

I hope we go forth on a two-track process at the same time, and again, the kind of schedule I would hope for and have encouraged Mr. Gonzalez to pursue is a markup that would have us out of the Banking Committee by the end of November and on to the House floor in early next year.

Can I just mention one other thing, a different issue, a matter of CDBG's. I am going to ask you to take a minute and use a real simple example so we might all understand it, explain how the CDBG program now works in terms of the low mod requirements for applying the funds, how it works now, why that is not the best of all worlds, and how you might change it.

Again, I am going to ask you to do so by use of an example.

Mr. DELLIBOVI. Let me just begin by explaining the program. It is largely a block grant program, as the name implies. The localities have broad discretion for what they can spend the Federal funds on, what activities they can use those Federal funds now, and basically they are allowed to spend up to 40 percent of those funds on activities which may be worthwhile and certainly are legal, but that do not benefit low-and moderate-income people.

We want to change that 40 percent to 25 percent. In other words, what Secretary Kemp is proposing to do is instead of having 60 percent of the money go to low- and moderate-income people, he wants to raise it to 75 percent; and the reason is that we feel very strongly that the needs of poor people, the needs of housing in the old neighborhoods come higher, at a higher level than replacing sidewalks.

Let me explain to you, to give you some examples of the kinds of activities that we do not believe are as high a priority as helping the poor people.

For instance, \$141,000 used to create community gardens from vacant lots in a neighborhood that had terribly run-down housing. That should have been used for housing. Seven-and-a-half million dollars of loans were used to rehabilitate apartments that were not occupied by low- and moderate-income people in New York City.

Facade improvements, \$718,000 for improving buildings that were not occupied by low-income people. We have improved and constructed restroom facilities at baseball stadiums.

Now, certainly no one would argue the need for restroom facilities at baseball stadiums, but the question is, is that what a poverty program is supposed to do? It's these kinds of activities.

We spent \$17,000 to construct barns for horses in Los Angeles. Now, the horses in Los Angeles may very well have needed barns, but that is not the kind of housing that Jack Kemp believes our money should be spent on, and we want to target it to the poor people, to the housing needs of people, not horses.

Mr. WYLIE. Will the gentleman yield?

Mr. CARPER. Yes, I will.

Mr. WYLIE. You are on to something there. I have asked questions and we have gone over this before for the community development block grant.

You are talking about increasing from 60 to 75 percent the overall low- and mod-benefit requirements. At no time this morning have I heard anything said about providing more effective targeting of funds in more affluent communities by providing 100 percent of all the activities of low-mod.

That is the part of it that concerns me more than increasing the 60 to 75 percent. I don't know if the gentleman from Delaware was getting to that aspect or not?

Mr. CARPER. Where I was going to go was to another part of the proposal. I understand the terms proportional accounting figure into—proportional accounting figures into the recommended changes for CDBG's.

It is not clear to me—I understand the decrease from 40 percent to 25 percent in terms of the amount of monies that can be used to serve other than low- and middle-income groups. But the term "proportional accounting"?

Mr. DELLIBOVI. Well, the current counting methods that are used under the regulations do result in—you have to understand, a given census tract or a neighborhood, or even a project, a particular building may not benefit only low-income people because there may be mix in that project.

We find even with a 60 percent requirement, some communities are only actually benefiting 50 percent poor people.

Mr. CARPER. Let me just back up again.

Currently it is my understanding it must be substantiated something like 51 percent of the residents of an area served with CDBG funds lower income?

Mr. DELLIBOVI. That is correct.

Mr. CARPER. Once that is substantiated this entire project can be applied to the overall low-mod requirements.

Mr. DELLIBOVI. That is also correct.

Mr. CARPER. That is 60 percent of the CDBG funds used to serve low- and moderate-income people? That is the way the program currently works?

Mr. DELLIBOVI. That is correct.

Mr. CARPER. Secretary Kemp is interested in increasing the overall low-mod to 75 percent and supports the concept of, quote, "proportional accounting," close quote, whereby if a project serves only 52 percent of the low- and moderate-income people, only 52 percent of the project could be applied to the overall low-mod benefit. That is what I don't understand.

I was hoping you could explain to me and to the others on the committee. I was asking you to use a simple example to explain how that might work.

Mr. DELLIBOVI. You are going to test my mathematical skills, but it may be that one—

Mr. CARPER. Use \$1, \$100, \$1 million.

Mr. DELLIBOVI. Let's try two, \$100 projects. One may benefit low-income people 100 percent.

The other may benefit low-income people 40 percent. Of the \$200, \$140 is benefiting low-income people. That would be 70 percent benefiting low-income people. That would pass the 60 percent threshold, but it would not pass the 75 percent threshold.

If on the other hand, you had two projects, one for \$100 and it was benefiting 100 percent low-income people and the other for \$100 and it was benefiting 10 percent low-income people, that would be \$110 going to low-income. That would be 55 percent of the benefits, and that would not meet the 60 percent threshold. It is a mixing.

We do look at the total program of the projects and the benefits in the program or projects for that year.

Mr. CARPER. My time has expired.

Let me ask that you look more closely at what I am trying to get to in the notion of proportional accounting. If you find there is something you need to say to me that you have not said to me here, share that in writing.

I appreciate it.

[The information pertaining to proportional accounting can be found on p. 332 in the appendix.]

Chairman GONZALEZ. The Chair recognizes the distinguished colleague Mr. Nowak of New York.

Since he was one of those initially bringing to the attention of the committee the questions arising out of the section 8 moderate rehab in, I believe in Buffalo.

The Chair would like to ask our distinguished colleague if he wishes to be recognized, if he has any statement he would like to make?

We appreciate your appearance here.

STATEMENT OF HON. HENRY J. NOWAK, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK

Mr. NOWAK. I thank the chairman for the courtesy. Certainly I don't want to take the time of the committee and their deliberations at this point in time.

But I appreciate the response that we did receive from the committee in looking at the Buffalo problem, which I think has been to some degree addressed by the reforms that have come out of HUD and Secretary Kemp, we would only urge we look forward to seeing the effect of those reforms and the legislation which is forthcoming.

I think what happened in Buffalo has happened throughout the country. As the chairman rightfully pointed out, he is looking at an overall reform.

I would expect that the specific instance and impact of the reforms on Buffalo would also serve other cities. So we will be following this with the chairman and with the committee as we move forward to make sure that the reforms do have the desired effect throughout the country.

I thank the chairman for his courtesy.

Chairman GONZALEZ. Thank you very much, Congressman. That was a very good statement.

I would like to have you consider yourself as an associate member of the committee. We will make available to you the material and documentation we have so that you can examine it.

We will need your help when we get to the House floor, so we want you to be acquainted and also welcome your suggestions.

Mr. Kennedy.

Mr. KENNEDY. Thank you, Mr. Chairman.

I have a few questions that surround specific changes Mr. Kemp suggested in his written testimony today.

The FHA 18 proposal would change the requirements governing disposition of HUD held or HUD owned multifamily properties. Your proposal would result in fewer low-income families being helped when FHA sells the property or when HUD sells the property that it owns.

There were some, I think, some factual inaccuracies in the written testimony that would suggest that somehow or another that HUD has only an obligation, or has an obligation, rather, to make certain that once these properties come into HUD's ownership, that 100 percent of those units have to be filled with low-income people.

I would just refer you to subtitle C of the multifamily housing management and preservation act which goes through very specific categories which would not indicate that this is the way the program works.

The obvious implication, Mr. DelliBovi, is that difficulty is that you are asking us to approve a process where we are getting rid of more units that could go to help poor people.

Mr. Kemp's indication has been he wants to make sure programs are designed to make sure poor people are protected. I wonder whether or not there are additional funds HUD would have available that could enable you to dispose of these properties, considering the fact that I am aware of specific instances where you have lowered the price down to \$7 or \$8,000 a unit to make sure they get out into the private sector. Those are going to for-profit developers.

Mr. DELLIBOVI. Mr. Kennedy, the specific proposal that we envision in FHA 18 is designed to deal with the problem that as the law now stands, if we dispose of a property, a multiple dwelling, multifamily property, we have to provide subsidy to go with it in the disposition.

There are some markets, and they are not in your district, I can assure you, where no subsidy is needed because the market rent is so low, so subsidy isn't really needed in those markets.

We would like to—

Mr. KENNEDY. If the properties are that low in value, can't the tenants, in fact, afford the properties.

Mr. DELLIBOVI. That is right. They do not need subsidies. We would not like to be forced to provide subsidies there because we would rather take the subsidy—

Mr. KENNEDY. The law does not require you to provide that subsidy?

Mr. DELLIBOVI. It now does.

Mr. KENNEDY. The law says that the Secretary shall not take less than one of the following actions. Either a section 8, the second

would be purchase money properties, third would be reducing the selling price, and fourth would be other financial assistance.

For instance, we have got a new bill here in the Congress, the Community Housing Partnership Act which has \$500 million which could be used to make sure those properties go into nonprofits and are permanently in the use of low-income people.

It just seems—the only point I am trying to make is we are trying to be helpful in terms of supporting some of the changes.

I want to make certain we are not inadvertently going to be harmful to poor people as a result of the changes you are suggesting.

Mr. DELLIBOVI. You are referring to single family homes?

Mr. KENNEDY. Multifamily homes. If you read the statute, you can review it. There are inaccuracies in the testimony today. I am just pointing out to you—

Mr. DELLIBOVI. We will go back and review that. As you know, Mr. Kennedy, Secretary Kemp believes very strongly, as you do, that we should encourage low-income people, tenants, neighborhood organizations, that kind of thing to get involved.

We certainly would not want to leave you with the impression that anything we are going to put into legislation will be an obstacle to that.

Mr. KENNEDY. Yes, sir.

I am just pointing out to you some inaccuracies that we picked up. I am sure you will go back and check them out and fix them up.

Another question I have pertains to Mr. Kemp's testimony this morning which would indicate you want to set aside about, I think it was one half of 1 percent, to increase your monitoring on oversight responsibilities.

I would just point out under the section 8 program, a \$10 billion a year program, that would set aside \$50 million to monitor that program. Under CDBG, that is about a \$4 billion program at 5 percent, that is \$20 million.

I assume you are not wanting to spend \$50 million on section 8 and \$20 million on CDBG.

The question becomes what proper role do we have in terms of making sure that those funds are being spent wisely.

Mr. DELLIBOVI. That is an excellent point. We would set aside the funds make them available to be used on a task order basis.

They would not necessarily be used in that particular area. The remaining funds would be recycled later in the year to go out to the beneficiaries, to the grantees.

Mr. KENNEDY. Do you think it would be possible to give us a better estimate on the specific programs where there are such large dollars involved and a better targeted perspective on how much funds will actually be used or needed?

I don't think anybody wants to think that you can spend \$100 million to oversee how HUD spends its money?

Mr. DELLIBOVI. You are right. We are developing that information. We will forward it to the committee as soon as it is available.

We use that as a target suggestion, but it is our intention to conserve whatever funds are available for that monitoring purpose

and to use the balance to recycle then the next year's funding round.

By the way, that is done in other Federal funding programs, including some transportation programs I previously managed.

Mr. KENNEDY. My last question has to do again with CDBG and the discretionary fund. As I understood the testimony this morning, the technical assistance funds that are part of the CDBG funding at the moment would be eliminated under the Kemp proposals. Obviously, we don't want to be blaming the victim, once again.

It seems to me that technical assistance money under CDBG has been effectively used by poor people in the past for the purposes of assisting poor people, I should say. I wonder why they have to be punished for this type of abuse.

Is there some—do you have some thoughts? Can you explain a little bit more about why the technical assistance portion is going to be denied?

Mr. DELLIBOVI. The reason we wanted to deny the technical assistance portion as it is now instituted is that it was a discretionary program subject to abuse. We believe we can build technical assistance provisions into the other existing programs so that we can still be providing in a competitive basis to qualified local organizations technical assistance but not do it out of a central fund.

I will be honest. It was a very tough call. But on balance, we concluded that the only way to eliminate the problems with these discretionary programs was to eliminate the discretion.

Mr. KENNEDY. I don't think, Mr. Chairman, that we want to continue the possibilities of blatant abuse. On the other hand, I think you are aware that these are projects that have been spent well in the past.

The question would be whether or not you can, perhaps, provide the committee with additional information about how that technical assistance is going to continue to be made available to people so that people don't read the testimony and think the technical assistance is now out the window simply because of the abuses that have taken place in the past.

If you could just perhaps between now and the next time you come before the committee prepare for us a better definition of how those changes are going to take place, I would certainly appreciate it.

[The information in regards to technical assistance can be found on p. 334 in the appendix.]

Mr. DELLIBOVI. We will be pleased to do that, Mr. Kennedy.

I want to make clear that we recognize the legitimate role for technical assistance and want to provide it fairly and in a way that it continues to be effective.

Mr. KENNEDY. That is terrific. The only point I am trying to make to you is I agree with that as a general theory. The question is going to become how that evolves into general, direct policy.

I think the committee's jurisdiction is making sure that continues in a way that it is helpful to the most vulnerable people in this society.

Thank you.

Chairman GONZALEZ. I'm very much concerned, gentlemen. The CDBG discretionary fund has been the sole source of community

development funds for the Indians. The history of legislation to assist Indians is quite sad, and I would not want to see any further renegeing on our commitments to them.

I have been one of the leading proponents for adequate Indian housing and community development assistance, even before I became chairman of the Housing Subcommittee.

It took many years for Congress to provide a HUD housing program for Indians. Well, I think we specifically provided something in 1962, if I remember correctly. Then, when CDBG was created in 1974, the Indians were initially left out. As I recall, in order to correct this, several years later, we made clear that they were to be CDBG recipients which is how they ended up being funded through the Secretary's Discretionary Fund. Currently, Indian CDBG amounts to some \$27 million annually.

What are you going to do about this?

Mr. DELLIBOVI. We are going to propose that Indian assistance be provided as a separate Indian program. It would be a separate line item in our budget submission. It would continue—the Indian portion would continue as it now does, but it would no longer be mixed into this slush fund of discretion. It would be separated and clearly directed to the purpose, as you pointed out, that is very well intentioned, and that we want to continue.

But we can continue doing those good things without continuing to do them out of the Discretionary Program. That is our intention.

Chairman GONZALEZ. Well, we want to make sure that we definitely provide for Indian CDBGs.

We do not want, with the best of intentions, to do away with a program that essentially, from a programmatic standpoint, has worked. This bothers me quite a bit.

So would a continuation of Indian CDBGs be incorporated in what you hope will be the secretary's legislative package?

Mr. DELLIBOVI. Absolutely. We intend to preserve those things that are working. We intend to build upon those successes and cast aside the things that didn't work or the things that discredited the program.

Chairman GONZALEZ. Mr. Hoagland?

Mr. HOAGLAND. Thank you for recognizing me, Mr. Chairman. I want to thank the two of you for being here so long and enduring these questions. Particularly, I would like to thank Secretary Kemp for his recent trip to Omaha. We had a very constructive tour, I think, of our housing authority in Omaha.

Secretary Kemp was in town for about a day or so and made a number of appearances. It was very beneficial, I think, to the housing community in Nebraska.

I've reviewed your plan prior to the hearing. I think it is a good plan and would like to let you know that I know many of us on this side of the aisle are here to help you implement it as quickly as possible.

I think we have a lot to learn from the past, and I think you all have done a good job of putting together a plan that will help us avoid these sorts of problems in the future.

My interest as a freshman member of this committee is, as much as anything else, to look to the future. In Omaha, we have a small community, small enough that it is the sort of community you can

really get your arms around. We do have some serious housing problems, some serious drug problems, some serious poverty problems in Omaha.

I would be interested in a nuts-and-bolts briefing from the two of you as to what kind of programs are available at HUD for the future, assuming the passage of your reorganization package, and what sort of programs we in Omaha should look towards applying for that might be beneficial in helping us in our long-range goal of solving our housing problems and eradicating poverty in our part of Nebraska.

Mr. DelliBovi, maybe you could go first and just give sort of a primer basic review of the kind of programs that communities the size of Omaha are eligible to apply for.

Mr. DELLIBOVI. Well, we envision that certainly the programs in place will continue to meet the needs of public housing residents who live in publicly owned and publicly operated housing. We have proposed very little change in the comprehensive assistance program for those folks.

We continue to believe in the strength of vouchers. We find that project-based certificates and vouchers led to abuses, though. We think the tenants should have the right to use those vouchers in the housing of their selection.

We don't believe somebody who is a poor person who gets Federal assistance should be sentenced to living in a project which may become neglected. We have an example of that right here in Washington, DC, at Tyler House, where poor people are forced to live in terrible conditions because the certificates they have are only usable in those particular projects.

We see those basic programs continuing. Community Development Block Grant with the changes we have made, we believe those changes will encourage the kinds of activity that Mr. Wylie referred to and that I saw firsthand in Columbus.

We also believe that the targeting of Community Development Block Grant funds more appropriately to public housing may do something about the tragedy we see in Cleveland, where there are thousands of run-down units of public housing and mismanagement.

We want to be able to continue to provide technical assistance. The tragedy of homelessness continues to be high on our agenda. We want to match the vouchers with local services that are available because we recognize it is not enough for a homeless person to just put a roof over their head and four walls around them. They are probably homeless because of some other crisis, some other problem.

I was in Kansas City yesterday announcing a new pilot program with Senator Bond, which will take vouchers and marry them to local services, counseling, education, job training, day care where necessary, so people can put their lives together and get back on the road to the American dream that we all share.

That is home ownership for as many Americans as is possible. We will continue to promote tenant ownership and tenant management of existing public housing. We recognize the committee's concern that we not eliminate all rental housing and eliminate the

availability of it. We believe we can help tenants manage the projects, manage their own lives and get to own their own housing.

Those are basically the agenda items we have set forth. Of course, there are drugs. I am going to ask the general counsel, Mr. Keating, to deal with that since that has been his special area of responsibility which the Secretary has designated for him to coordinate completely our anti-drug efforts in the department.

Mr. KEATING. We would all be well served if we could duplicate Bob Armstrong, your housing authority director, throughout the United States. If we had a Bob Armstrong in all 3,300 public housing agencies in America, we would all be much better off. I know Secretary Kemp uses him as a symbol of how a properly run, properly led, creatively run and led housing authority should be managed.

One of the things Secretary Kemp did when he came to HUD was for the first time create a drug office, a drug policy office at HUD. He made the director of that office a lady by the name of Julie Fagan, who chaired the Communities for Drug Free Colorado program, Governor Romer's executive assistant in the Colorado experiment which was successful.

We are now implementing the 1988 act, a requirement we have a clearing house, a requirement we have regional training. We have also, as a result of the experience of the Secretary requesting information from all 3,300 public housing agencies about what they are doing about drugs, are in the process of compiling a resource book of all the best and brightest ideas for the tenants to address and the public housing authorities to address the drug scourge.

The Secretary is very anxious that security be provided first to tenants, that public housing be drug free. The public people in public housing have the same rights as people in private housing to be rid of their drug dealing neighbors.

First, he has waived the lease and grievance process in a number of States that have due process State court systems for the eviction of tenants accused of drug and drug-related activities. We are in the process of trying to do the same thing in section 8 or subsidized housing.

Throughout the United States repeatedly the Secretary emphasized at the top of the list of six agendas a drug free environment and is aggressive in working with tenant groups, the neighborhood leaders, civic leaders, community leaders in attempting to address this problem.

We anticipate in the very near term, we will have a much larger announcement bringing in the public sector, private sector, Members of Congress, community leaders to help us address this problem.

Mr. HOAGLAND. Thank you for your answer, Mr. Secretary. I know my time is up.

I would like to visit with you about the free enterprise drug zone concept on how that might apply to Omaha.

Thank you, Mr. Chairman.

Chairman GONZALEZ. Mr. Schumer.

Mr. SCHUMER. Thank you, Mr. Chairman. Let me apologize for being late. I had a longstanding commitment in New York.

My questions will fall into two areas. First, I have one which really relates to the issue of dollars. I would say to Mr. Hoagland, the one construction program that puts roofs over people's heads that was proposed here is the voucher program, a program I disagree with, but so be it. Let's have our disagreements.

If in the next budget the administration requests the same amount of vouchers as this year, the city of Omaha will get on an appropriated basis about 47. There will be 47 households taken care of.

I guess I would say to my good friend, the Under Secretary, and I would say it to the Secretary himself, for a year or almost a year, we have really welcomed the initiatives, the interest and the spotlight on housing that the Secretary has provided. But the ultimate test for the Secretary and for HUD is going to be can you get more dollars, because there is no way with all the reforms in the world, and they are important, that we are going to put roofs over people's heads without more dollars.

I, for one, just being one Member, would say I am going to carefully scrutinize the next budget that the President submits. And if we don't have more dollars, it is going to be very disappointing to the low- and moderate-income people who need housing, and I think it will make all of us think twice about how successful this administration is going to be in carrying out all the words that we have heard.

I would now like to get to the area of reform and then I will come back to the dollars. Again, as the Secretary knows, I think the Secretary has been terrific in the area of reform in terms of his outspokenness, in terms of his admitting a problem and trying to deal with it. But I am a little perplexed right now on a couple of scores.

First, we don't have a legislative proposal from the Secretary, from HUD. It is optimistic at best and unrealistic at worst to expect the Congress to approve this unless we were to just be a rubber stamp within a month when we are going to leave here.

I think the chairman has said he will make every effort to try. But it is going to be strategically difficult to get a package of reforms through, put down on our desks on October 18, the earliest, when session is expected to end in November.

That is maybe no one's fault, but this idea that, you know, we have to vote on them within 2 days of the proposed reforms is unsettling to me, even though I welcome the Secretary's work. So it leads to my question, of the 44 reforms proposed by HUD's own admission, 17 could be administratively implemented.

Our analysis or the analysis that I have here, is that another seven, what you call legislative. But there is no statute—nothing in the law that would prevent you from doing these administratively. They contain EFT-1, ETH-1, ETH-2, public disclosure of allocation and funding decisions, ETH-5, sunshine waiver of regulations, MRD-2, appointment of chief financial officer and comptroller of FHA.

My analysis, it is pretty clear you could do those as well as the other 17 administratively and that would end up being the bulk of your package. Admittedly, if Secretary Kemp would move on, a future Secretary could undo them.

Instead of pounding the table and saying Congress has to do these within 3 weeks or 4 weeks, why don't you administratively implement them right now?

Mr. DELLIBOVI. We are administratively implementing each and every one of them to the extent that we can. The 17 that we have identified, we are looking at all of the balance of them.

If there is any one of the others or all of the others we can do administratively without legislation, we will do so. Some of them may require regulations and not legislation. However, we do believe our job is not just to clean up HUD for the time that we are there, point of fact.

We would not need legislation or add—we are going to run this thing right while we are there. But we are temporary tenants of these offices at 451 Seventh Street. It is important that we leave that institution running right and that it not be subject to abuse in the future.

Mr. SCHUMER. Mr. Under Secretary, I understand that completely. No one is saying we shouldn't do these statutorily. If you can do the large majority of them administratively, saying Congress has to do this by November 15, its adjournment date, we shouldn't do anything else.

We can adopt them. I guess my question is how many of the 17 you say have been administratively put into effect thus far?

Mr. DELLIBOVI. We are acting as quickly and as immediately as we possibly can. I will supply for the record and exact breakdown of each of them and the status of each. Let me just point out that in no cases are we proceeding in the old way of doing business.

We are beginning and we are at the threshold of a new fiscal year, so we intend to put sunshine on all of the funds that are appropriated and all of the funding rounds for fiscal year 1990. We will implement each and every one of them as quickly as we can.

Mr. SCHUMER. Do you have any time frame as to when any of them will be actually in effect?

Mr. DELLIBOVI. We are in the process right now, for instance, on the chief financial officer, of beginning the efforts to recruit, of creating that position, doing the internal job description work. We are about to sign a contract with the National Academy of Public Administration to help us design the structure of that organization.

So we are moving out on that one. We have begun reform in the area of discretionary and headquarters reserve funds that were left over. We have imposed competitive standards on all of the allocations decisions that are underway. We have in the area of, one of the areas of questioning before your arrival here today was the statutory use in our legislation that would propose the measuring of low income tax benefits with HUD program benefits.

And our housing commissioner, Austin Fitts, has already begun to do that administratively with the funds that are now available. She began that effort I would say in June right after we became aware of that double-dipping problem. So we are acting on each and every one of them administratively as we can.

Mr. SCHUMER. Let me ask you a question. Are there any of the major reforms that you continue—I mean I have given you a list here of the seven that I thought you listed as legislative. Maybe you just prefer to do it legislatively, but you could do it administra-

tively. Are there any of the major forms that you proposed that you couldn't do without a statute?

Maybe Mr. Keating should answer that.

Mr. KEATING. Mr. Chairman, I am afraid I can't say every one of them, but I can look, for example, at the ethics package and give you, for example, civil monetary penalties, ETH-7. Any penalty associated with any of these, for example—

Mr. SCHUMER. All the penalties.

Mr. KEATING. Would require legislation. As the Under Secretary has indicated, a number of bankruptcy, CDBG, a number of those things will require program evaluation and amendments under management, rule-making under FHA. There would be a number.

Mr. SCHUMER. A few of them. You agree most of them could be done administratively. Do you have any disagreement with those I mentioned?

Mr. KEATING. I would say a significant number of these can be done administratively. As Mr. DelliBovi indicated, we are running on a parallel track. We would like to permanentize this. This is the package that went to OMB last night. We have a substance reform bill that we drafted in-house for the purpose of their review.

Mr. SCHUMER. We have no disagreement that while the legislative process, awaiting, of course, the submission of them to us, wins its way that a large number of them could be implemented by regulation?

Mr. KEATING. We will attempt to—

Mr. SCHUMER. It is a large number?

Mr. KEATING. Yes.

Mr. SCHUMER. It is a large number?

Mr. KEATING. Yes.

Mr. SCHUMER. None of the ones I mentioned, at least, initially come to mind as having any problem doing them administratively?

Mr. KEATING. I don't think so.

Mr. DELLIBOVI. If I may comment, Mr. Schumer?

Mr. SCHUMER. Yes.

Mr. DELLIBOVI. We would be more comfortable in a week to 10 days after our assistant secretaries have been able to analyze each and every one of them. I have asked for a report from each of them telling me exactly that.

If they can do it administratively, if not, why not. If it is a regulation, if it is a law—

Mr. SCHUMER. You will have to publish the regulations and await comment as well. So you can't do that immediately. But you know we are going to be out of session from Thanksgiving until the end of January. It takes a month or two for the process to get going. I don't know it as a major barrier in at least getting most of them implemented.

Mr. DELLIBOVI. We are not able to change regulations while you are not in session. That will tie us up with regulatory package because we require a time table of legislative days. That becomes very cumbersome.

Mr. SCHUMER. Right. The next question does go back to the money issue. You have already indicated some of the things that will be in your new program, the budget submission. What are the odds that we will see more money in the housing functions in the

budget submitted by the President for fiscal year 1991 than we saw from fiscal year 1990?

Mr. DELLIBOVI. Mr. Schumer, I am neither a betting man nor am I the Director of the—

Mr. SCHUMER. You are a very bright man, and I have known that for the 20 years we have known each other.

Mr. DELLIBOVI. I am bright enough to know I shouldn't make the budget announcement. That is the President's prerogative in February.

Mr. SCHUMER. Do we have a good chance of getting more money?

Mr. DELLIBOVI. I believe we have an excellent chance of getting the money we need to get the job done.

Mr. SCHUMER. That is a relief because I don't think you can do that. I don't think anyone, even Jack Kemp, can get that done.

Mr. DELLIBOVI. The question really isn't just one of money. The question is the benefits that are provided. How many more families can you provide housing assistance to? What is, to me, so disappointing about the money that we have authorized and appropriated is that so many poor people see all this money being propagated and they don't see any improvement in their lives. You see millions of dollars allocated to public housing authorities in Cleveland and Washington, DC, and yet they can't turn a unit around and make it available.

Mr. SCHUMER. You need both. But I want at least to say, to state for the record and give you folks notice, and I think there are a lot of my colleagues who agree with this, that if you don't have significantly more money, you are basically rearranging the deck chairs on the Titanic. We can argue about whether the vouchers work or not, we can argue about other things, but I don't think we can argue that for the millions of people who are unhoused, the \$9 billion or so of assisted housing in this year isn't enough, not even close to enough.

I would be unrealistic to think next year you are going to lift it to the 30 or \$40 billion you need to give each one of them help. My own point is I at least hope to focus the spotlight on money as well as the other issues. I hope you will be successful.

One final question. Co-insurance, it seems to me that the co-insurance program is basically unreformable; that because you gave such a large incentive up front that the profitability of the private co-insurer and the profitability, if you will, or the lack of loss that the Government would undertake don't match up.

For instance, in the present co-insurance program, if the up-front fee is 5 percent and the private guy takes 20 percent, he or she could undertake five properties, have one of them fail, and still make money, whereas the Government, with those same five properties and one failing would lose its shirt. And it seems to me that the only way to rectify that is to bring the fee down so low or the percentage that is insured privately so high that you won't get any takers. And my question is how do you overcome that dilemma?

Mr. DELLIBOVI. We believe that co-insurance can be saved if we institute some very basic and sound business practices.

Higher minimum capital requirements for the lenders, for instance, higher cash requirements for the developers, improved underwriting standards. Basically sharing the risk.

We have an internal task force that is working through that problem and about to make specific recommendations to the Secretary.

We believe, as the Secretary mentioned earlier this morning, that no co-insurance program will mean no multihousing program.

That co-insurance is providing a role and that we can save the program. We recommend there are going to be more losses.

If we closed down the program, we would continue to incur substantial losses. Commissioner Fitts is committed to bringing about the kinds of reforms that will enable us to stem the losses and still save the program.

It is our analysis, because co-insurance is, or insurance is so vital to multifamily housing that we need to do everything that we possibly can to resolve that dilemma.

It is going to be a tough one, but our staff feels that it is a challenge we can meet.

Mr. SCHUMER. The mod rehab program, is eminently more savable and reformable than the co-insurance program. I don't quite understand why the one has been slated for elimination when most of the problems in it were not the structural problems, but rather the political problems that we have all unfortunately seen too much of.

Where it seems to me the co-insurance program problems are basically structural.

Mr. DELLIBOVI. In our reform package we will have a program to meet the needs of moderate rehabilitation.

We certainly are cognizant of that need. We just do not believe that the existing program is one—

Mr. SCHUMER. You are not intending to say mod rehab will be replaced by, say, vouchers? I know the Secretary and you are looking for new approaches. We have had a stand off between the administration and Congress about vouchers.

Every time they dismantle a program, they say they will replace it with vouchers. Vouchers don't build housing.

I hope there will be a real program put in place as opposed to simply the fig leaf of saying we are replacing every program with vouchers.

Mr. DELLIBOVI. The Secretary said repeatedly he does not want to be the Secretary of Vouchers. At the same time, we recognize that vouchers provide an increase in assistance to families in the housing assistance.

If you look at the number of families being assisted, how many families were being assisted in 1981? It was about 3.1 million families. Today it is about 4.3 million largely because of families.

We have more families receiving housing benefits today due to vouchers. Vouchers do not in themselves produce new units, but they do provide a revenue stream.

We believe we can build in that revenue stream to provide the supply of housing that is necessary.

Mr. SCHUMER. I would just say to the Under Secretary—I don't want to get into a contentious dispute on the facts here, but I would be surprised if there were more than 200,000 or 300,000 total vouchers outstanding.

Mr. DELLIBOVI. It is not just vouchers. It is vouchers, certificates, it is the whole basket of programs. The point really is when everyone talks about cuts in programs, they lose sight of the fact that most of the cuts were in a new construction program and that we do have more families benefiting from the Federal housing programs, the entire basket of them.

Vouchers, certificates, 202, whatever it is. That is a record that we are proud of at HUD, that our employees, most of whom are career people, who are not involved in any illegitimate activities. It is a record we take pride in and I think the committee should, too.

More Americans are receiving housing benefits. We ought to recognize that and not run away from that reality, which is good news.

Mr. SCHUMER. I would say most of the reason more people are receiving housing has been because of the programs passed both under the Nixon and Carter administrations in the 1970s, and they are still in there.

The amount that has been added in the 1980s has been rather small.

Furthermore, the 15-year programs, the section 8 certificates and section 8 program is all going to start expiring.

That will undo the record that was stated before. I just hope you folks will call for renewal of those things even though they are fairly expensive. Otherwise we are going to see the actual numbers go down.

Mr. DELLIBOVI. I don't know if we will call for complete renewal of the Nixon programs or Carter programs.

Mr. SCHUMER. I am talking about starting in this fiscal year.

Mr. DELLIBOVI. We are very concerned about expiring certificates. The administration is committed to the renewal of those expiring certificates. If you could read my lips, that would obviously mean there is going to have to be an increase in the amount of money that is requested in the budget.

I didn't say it, but you understand that there is no way we can be committed, and we are, to that and run away from the price tag that is going to be required to renew those certificates. We are committed to renewing those expiring certificates.

We are similarly going to be committed to developing programs that meet the need in tight markets, such as the one in your district and my old neighborhood in Queens. We recognize that the existing programs do not meet those needs and that something has to be devised.

I might point out one of the things we see successful in Mr. Wylie's district is the use of CDBG money in neighborhoods like that.

I certainly am hopeful that in our home town the city officials will make better use of those available funds in neighborhoods like ours. I have talked to Commissioner Biderman about doing just that.

Mr. SCHUMER. I don't want to keep this going on forever. I think it is good news you are going to extend the certificates. I read your lips, and that, too, is good news. CDBG has been cut and cut and cut. It is supposed to now cover so many programs, that is awfully hard to say new housing money will come out of them.

In New York the CDBG money is spent very well and to good purpose. I, for one, we have been up and down that hill 9 years in a row now, too.

We are not giving you housing money, take it out of CDBG. That is not satisfying.

I am pleased with both your comments that the certificates will be renewed and secondly that you will look for new programs that deal with housing problems in tight marketplaces.

I thank the chairman and yield back my time.

Chairman GONZALEZ. Thank you.

Mr. Wylie.

Mr. WYLIE. Thank you very much, Mr. Chairman.

I am a voucher man, myself, Mr. Secretary.

I think the point needs to be made following Mr. Schumer's statements that we have heard some excellent testimony this morning.

It seems more clear than ever to this Member that we do need to move ahead quickly on a legislative package of reform.

The Secretary has said that reform has to be a joint effort with Congress. Although out of the 44, I looked through here, I think 19 of them probably could be administratively implemented and put into effect right away.

You can correct me if I am wrong, but I think the Secretary was indicating even some of those, he felt, ought to be put in legislative language so other Secretaries wouldn't have the discretion necessary to mess them up. If they are good reforms, maybe we ought to statutorize them.

We have learned from GAO reports that the FHA insurance program, which is very dear to my heart, is still operating with antiquated data equipment, as they said. You are quoted as saying, Mr. DelliBovi, that the problem is not that FHA has bad systems, but the systems can't talk with each other and you need to put more dollars into the reform of this system.

I realize money is tight, but I was thinking we could use the savings from the section 235 refinancing for additional staff or updating the computer system?

Mr. DELLIBOVI. We have been fortunate thus far with the Appropriations Committee supporting the beginning effort to design the system. Once we have the system designed, there is a tremendous lead time here.

Once it is designed, it may be an issue in paying for the equipment that is necessary. We are at the design stage now.

We have adequate funds to carry out that activity. These are very complicated systems. You don't just go down to the local computer place and pull something off the shelf, and that is the difficulty that we face. There is long lead time to get this right.

Mr. WYLIE. Just throwing out an idea. I know you all take it into account.

Thank you very much, Mr. Chairman.

I think we have heard some very excellent testimony.

Chairman GONZALEZ. Thank you, Mr. Wylie, for your tremendous help.

I did want to sum up by saying that Mr. Schumer, I think, referred to the money. That is the fundamental question. As an ex-

ample, in order to fund the additional, or the renewal of certificates, expiring certificates, we estimate that it will require an additional \$9 billion so that we do have very serious aspects of just that commitment alone with respect to the funding.

The fact remains, though, when it is all said and done that in just these months of this year, 1989, this committee has received more cooperation. We have had extremely good communications than all of the 8 years of the previous administration.

I think that is the truth. I wanted to express our gratitude for that. I have expressed it to the Secretary, but I think today's hearing caps it.

We are now in the month of October, and we have had more interaction, more communication in just these 9 months or so than we have had in the past 8 years with the prior HUD administration.

So we want to thank you very much. You have gone above the call of duty. You have been very patient. We are very grateful, but as Mr. Wylie said, this hearing has produced very valuable information to help us in our legislative endeavors.

So, thank you very much, sir.

The hearing will stand adjourned until further call of the Chair.
[Whereupon, at 1:50 p.m., the hearing adjourned.]

APPENDIX

October 12, 1989

OPENING STATEMENT BY CONGRESSMAN RICHARD LEHMAN
HOUSING SUBCOMMITTEE HEARING ON HUD REFORMS

October 12, 1989

MR. CHAIRMAN: I want to congratulate you on moving forward so quickly to enact housing reform legislation. I would also like to commend Secretary Kemp for being responsive on his watch and working to clean things up. We need to act now to insure that the violations committed under the Reagan Administration are corrected, and that a scandal like this will not be repeated.

Secretary Kemp, the package you have put forward is a good one. While many of the management and FHA reforms can be addressed administratively, your proposals to improve ethics and end influence peddling will require legislative action. I support your efforts to eliminate discretionary spending, and I believe your proposals to impose fines on lenders who violate FHA or GNMA rules and to empower the Inspector General with subpoena authority will put some enforcement behind HUD policies. I also agree that better oversight is clearly a high priority and one which should be implemented immediately.

I believe we have to keep in mind as we progress along this path that HUD reform is not the only housing issue which needs to be addressed. Chairman Gonzalez has sponsored H.R. 1180 which would reauthorize vital housing programs which have been greatly effective in meeting the housing needs in this country. The continuation and support of these programs should go hand in hand with HUD reform.

Despite the daily headlines exposing more and more travesties at HUD during the Reagan years, it should be remembered that much of this results from the scarcity of funds created by the severe decline in the housing budget in the past eight years. HUD reform can not be successful without a revitalization of the housing programs needed to solve the housing problems currently going unmet. These programs have worked successfully in the past, and should not suffer because of weak administration, slack ethics, and poor oversight by an Administration aimed at eliminating them. I encourage the new HUD under Jack Kemp to work with this Committee to not only correct the mistakes of the past, but to improve the prospects for the future.

STATEMENT OF THE HONORABLE NANCY PELOSI
SUBCOMMITTEE ON HOUSING AND COMMUNITY DEVELOPMENT

HEARING ON KEMP HUD REFORM PROPOSAL

OCTOBER 12, 1989

MR. CHAIRMAN: I COMMEND YOU FOR HOLDING TODAY'S HEARING WHICH WILL ALLOW SECRETARY KEMP THE OPPORTUNITY TO EXPLAIN TO US IN PERSON HIS HUD REFORM PROPOSAL. I THANK SECRETARY KEMP FOR TAKING THE TIME TO APPEAR BEFORE US TODAY.

I HAVE HAD AN OPPORTUNITY TO REVIEW THE HUD REFORM PACKAGE AND I FRANKLY AM CURIOUS AS TO WHY MANY OF THE SUGGESTED LEGISLATIVE CHANGES CANNOT BE MADE ADMINISTRATIVELY. I UNDERSTAND THAT SECRETARY KEMP HAS HAD HIS HANDS FULL TRYING TO CLEAN UP THE SCANDALS AT HUD, BUT I AM ALSO CONCERNED THAT LITTLE ATTENTION IS ACTUALLY BEING PAID TO ADDRESSING OUR NATION'S MANY HOUSING NEEDS.

WITHIN THE HUD REFORM PACKAGE, I AM PARTICULARLY INTERESTED IN PROPOSALS TO INCREASE CDBG TARGETTING, AS WELL AS THE DEVELOPMENT OF ANTI-POVERTY STRATEGIES. I LOOK FORWARD TO THE SECRETARY'S ELABORATION ON THESE PLANS.

LAST WEEKEND, TENS OF THOUSANDS OF PEOPLE PARTICIPATED IN THE HOUSING NOW MARCH TO EXPRESS THEIR INTEREST IN THE DEVELOPMENT AND FUNDING OF HOUSING INITIATIVES. NOW, WE HAVE BEEN PRESENTED WITH AN ELEGANTLY PACKAGED, COMPREHENSIVE HUD REFORM PACKAGE. WHERE DOES THAT LEAD US TO IN THE DEVELOPMENT OF HOUSING INITIATIVES? HUD REFORM IS CLEARLY NECESSARY, AND I WOULD SUGGEST THAT ^{much} ~~A LOT~~ OF IT CAN BE DONE BY THE SECRETARY WITHIN HIS OWN DEPARTMENT. ACTION ON HOUSING PROBLEMS IS ALSO

CLEARLY NECESSARY; HERE I WOULD SUGGEST THAT WE ARE ANXIOUSLY
AWAITING THE SECRETARY'S NEWS ON WHAT HUD WILL DO TO ENCOURAGE
DECENT AND AFFORDABLE HOUSING FOR ALL AMERICANS. THANK YOU.

STATEMENT OF SECRETARY JACK KEMP
BEFORE THE
SUBCOMMITTEE ON HOUSING AND COMMUNITY DEVELOPMENT
HOUSE COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
OCTOBER 12, 1989

Mr. Chairman, and members of the Subcommittee. I appreciate having this opportunity to appear before the Subcommittee to discuss with you the comprehensive reform agenda I announced last week to root out mismanagement and systemic flaws in HUD programs.

It is clear, Mr. Chairman, from your prompt scheduling of this hearing, that you share my sense of urgency about HUD reform. I look forward to working with you and other members of Congress to pass a legislative package of reforms that will, in essence "clear the decks", so that we can use the full resources of HUD to wage war on poverty, homelessness and despair.

The President and I do not and will not tolerate the systemic flaws and the ethical misconduct at HUD which have allowed our programs to be abused for political purposes or personal gain at the expense of those in need. We will not allow HUD's mission to be paralyzed.

It has been three months to the day since I last testified before your Committee on the problems at HUD. On July 12, I made the statement that using the full resources of HUD to empower the poor, expand housing opportunity and promote economic growth could occur only if integrity, efficiency and fair play are

returned to the Department of Housing and Urban Development. I said further that I was determined that all HUD programs should operate without favoritism and for the fullest benefit of those in need. I said that I intended to administer HUD programs competitively and consistent with statutory requirements, for their legitimate purpose.

Mr. Chairman and members of the Subcommittee, these are the standards that we have applied to our rigorous review of the operations of all HUD programs. We believe that we have acted vigorously and correctly to end the abuses which have plagued HUD's programs. The American people need to have the confidence that the Department of Housing and Urban Development is both willing and able to move forward on an agenda to create opportunities for homeownership, jobs and hope in our nation's inner cities and distressed rural communities.

Chairman Gonzalez, I am gratified by the bipartisan spirit in which you and Chalmers Wylie, and many other members of Congress have approached the past problems at HUD. Members of this Committee, including Marge Roukema, Chuck Schumer and Paul Kanjorski, as well as others in Congress, have made good and constructive proposals. Many of the proposals we have made in our reform package have drawn on those suggestions. We have also followed numerous recommendations made by HUD's Inspector General, the General Accounting Office, and HUD's many professional and dedicated employees, both career and non-career.

I especially want to pay tribute to the team we have

assembled at HUD. Under Secretary Alfred DelliBovi, Assistant Secretary for Housing Austin Fitts, General Counsel Frank Keating, and all of the fine team that President Bush and I have assembled at HUD are capable and dedicated public servants of great integrity. This package is in many ways a reflection of their commitment to the goals and principles which are at the heart of HUD's mission.

Mr. Chairman, some of the reforms which I proposed last week can be implemented unilaterally, and I will do so. Other changes will require legislative action, and the Administration will be transmitting draft legislation shortly. I look forward to working with Congress to enact these proposed legislative changes on an expedited basis. The various congressional reviews of HUD have been critical to the process of bringing our systemic and other shortcomings to light. And while I am certain that as we continue to work together on further reforms that might be needed, we have sufficient information on many of our problems to take action now. I am confident that the spirit of bipartisan cooperation will continue as we attempt to match our words with action.

The comprehensive reform package we announced last week envisions reforms in three basic areas: ethics, management and finance and the Federal Housing Administration. While I will not go into detail on each of our nearly 60 reform initiatives, I want to talk at some length about the major reforms which will have to be implemented.

First, Ethics. Most of these proposed reforms will require legislative action. Integrity and fair play are essential to restoring confidence in HUD and to ensuring that the resources of the Federal government go to assist those who are most in need of our help. Many of HUD's worst problems exist because entirely too many people at HUD decided that the rules of fair play did not apply. Much of the work done by HUD's Inspector General documented that housing subsidies had been awarded to certain developers who paid huge fees to politically connected consultants and lobbyists, people who did little more than open doors and place phone calls. Need and merit as criteria for funding decisions gave way to greed and favoritism.

The first reform in this package will establish a strict requirement that all consultants and lobbyists who represent those attempting to obtain grants from HUD must register with the Department. In addition, all those applying for funds will be required to disclose any fees paid to lobbyists, consultants or lawyers in connection with their application. In the past, politically connected consultants have received as much as \$1,500 per unit to arrange funding awards in advance of public notice. This reform will subject would-be influence peddlers to full public scrutiny, and we will establish civil penalties for non-compliance.

Because we learned that many past funding decisions were based on political influence rather than merit, we intend to require that from now on, all of HUD's housing and community

development assistance be allocated by formulas based on relative need through a competitive process, with objective criteria.

To reduce opportunities for abuse, it is essential that HUD's business be conducted in the light of the sun. All funding decisions will be publicly announced and published quarterly in the Federal Register; all awards will be fully documented for all to inspect. This reform will ensure that the taxpayer will be able to hold HUD accountable for every dollar spent.

A further "sunshine" proposal will be implemented in instances in which HUD program requirements need to be waived. In far too many instances, waivers and exceptions to HUD rules have turned into "black holes" that were manipulated to maximize someone's financial gain. The result of such waivers can mean excessive costs that endanger both the project and FHA. In one case in Chicago, HUD officials allowed a developer to undertake certain actions that led to FHA financing of a high-rise luxury apartment complex in which some units rented for as much as \$2,600 a month. The project failed and FHA was stuck with a \$50 million claim. In the rare cases where waivers are legitimately required, they will henceforth require the approval of an appropriate assistant secretary, and they will be published in the Federal Register.

Although there is some value to having a discretionary fund available to the Secretary, I have concluded that, in order to avoid both the appearance and reality of favoritism, the Secretary's Discretionary Funds for housing and community

development must be eliminated. We have no excuse for allocating scarce Federal resources on any other bases but need and merit. In the Bush Administration, and during my stewardship of this department, no decisions will be made at HUD for the political advantage or personal gain of anyone.

Second, Management and Financial Reform. It has become painfully clear that HUD's management systems severely lacked anything resembling rigorous financial accountability. This created great difficulties in our ability to evaluate the financial health and effectiveness of many of our programs.

Mr. Chairman, in recent testimony before your Committee, a representative of the General Accounting Office stated, "an important part of the solution to HUD/FHA's problems is to establish a Chief Financial Officer within HUD and a Comptroller within FHA."

We completely agree. I intend to create a new position of Chief Financial Officer, who will report directly to me and who will have the responsibility of overseeing HUD's financial operations. I will also appoint a Comptroller for the FHA. Moreover, I intend to contract for an independent management firm to identify structural and systemic problems and to recommend comprehensive reforms to strengthen the financial and managerial integrity of HUD programs.

As in the case of HUD's closing agent embezzlement episodes, there was inadequate attention paid to reconciling of accounts, management reports and cash tracking. No one person at HUD below

the Secretarial level was accountable for making sure that the different program offices and computer systems were working together to prevent fraud. Lack of accountability and responsibility will no longer be accepted as either reasons or excuses for poor financial management.

I want to touch on two proposed reforms which might be of particular interest -- and perhaps concern -- to the Subcommittee. First, we intend to propose an amendment to Section 7(o) of the Housing and Urban Development Act to permit more expeditious legislative review of all HUD regulations. While I recognize that the 7(o) process is a tool for oversight by the Banking Committees, existing procedures can subject HUD rules to extreme delays and, in light of our current reform initiatives, could hinder the Department's ability to institute necessary policy changes and statutory mandates.

Second, we propose to increase targeting requirements under the Community Development Block Grant (CDBG) program. We have come to realize that CDBG does not always focus its precious resources on low-income people. Counties with desperate need for jobs and housing have instead, all too often, directed block grant funds to wealthy suburbs for amenities which they could well provide for themselves and which are not intended to be provided under the CDBG program. Currently, grantees are allowed to spend 40 percent of their block grant funds on activities that do not benefit low and moderate income people. Because of counting methods, even low and moderate income projects may

assist a high proportion of non-needy persons, but are credited as benefiting the poor 100 percent. Our reform would require that the counting method used to credit low-mod benefits reflect the actual proportion of low and moderate income persons benefiting from the project, the overall low-mod benefit targeting requirement be raised from 60 to 75 percent, and that more affluent communities be required to spend all of their funds on projects addressing the priority of assisting low and moderate income persons.

To further ensure the goal of strictly targeting HUD's resources to those in need, I am asking Congress that up to one-half of one percent of all appropriations -- approximately \$100 million -- for housing and community development be set aside for program monitoring and evaluation. I am also asking for more authority to recover misused government funds from HUD grantees. And we will continue the aggressive efforts of our Asset Recovery Strike Force under the direction of General Counsel Frank Keating, which has recovered nearly \$4.5 million to date.

Finally, the Federal Housing Administration. We have concluded that the FHA requires sweeping reform. FHA's accounting and financial records have been so poorly maintained that they are indecipherable. As a result, from 1974 until earlier this year, no audits of FHA's financial statements could be conducted. I intend to require the FHA to publish financial statements on a yearly basis. These will be compiled and audited

by independent accounting firms.

FHA currently operates 47 different insurance programs and has \$300 billion of insurance in force, yet it currently has only one actuary. We have commissioned an independent actuarial analysis to help FHA managers assess the impact of changing economic conditions and other factors on the integrity of the fund.

In addition, the FHA's accounts, which have been lumped together indiscriminately in the past, will be broken out program by program, region by region, beginning in 1991, so we can have an accurate basis for accountability and decisionmaking.

In the past, because of our inability to judge whether our programs were properly targeted, HUD was unable to recognize that program funds were often benefitting developers and consultants instead of those who needed them.

Such is the case with the Title X program which was designed to provide FHA insurance for land development and intended to produce low-risk financing for builders who would develop housing for low and moderate income families. What was intended to be low-risk for builders and developers turn out to be high-risk for FHA. Half the Title X loans insured since 1977 have defaulted. Our largest Title X default was a California Country Club that included a \$7 million golf course with an \$8 million clubhouse, 17 tennis courts, 2 swimming pools and a health spa.

In July, I advised this Committee that I intended to eliminate Title X through rulemaking. I am now proposing what

some Members suggested was the more appropriate course -- eliminating it through legislation.

The FHA's single family insurance programs are the cornerstone of the Federal government's policy to meet the mortgage financing needs of low and moderate income families -- those who will actually occupy their homes. FHA was never intended to create opportunities for profit by real estate speculators and "no money down" operators. Yet, while investors made up only 2.5 percent of new FHA policies last year, they accounted for 15 percent of the losses. There is one investor in Denver who defaulted on all 750 FHA homes he owned. To correct this abuse, private investors as well as those who use FHA for second homes for vacation purposes will no longer be able to obtain FHA insured loans on these properties.

As everyone knows, abuses by private sector closing agents have been notorious. Our reforms will impose tough new standards on private sector entities such as closing agents, appraisers, lenders, servicers, and mortgage bankers, including requirements for licensing and bonding.

We believe that the coinsurance program, if it is properly reformed and administered, can make a contribution to the development of affordable multi-family housing. I am restructuring the program by raising entry, capital and disclosure requirements for coinsurers in order to correct the problems which have been responsible for at least \$1 billion in losses in the program. Another primary cause of coinsurance

losses was, purely and simply, the lack of will to enforce program requirements. I will insist on more stringent monitoring of this program by HUD managers.

Finally, the layering of HUD subsidies, such as Section 8 Moderate Rehabilitation and property disposition, on top of the subsidy provided for low-income housing development by the low-income housing tax credit has frequently resulted in huge and unwarranted profits for developers. We intend to stop the windfall profits that result from this form of double-dipping by tightening our procedures, in conjunction with legislative reforms in the reauthorization of the LITC, to ensure that scarce resources are used to maximize the number of units developed, rather than to subsidize consultants and developers.

Mr. Chairman, these reforms, as a whole, represent a fundamental redirection of the Department of Housing and Urban Development -- a redirection back to the poor and the tenants and the community-based nonprofits, and the wisdom, ingenuity and entrepreneurial spirit they demonstrate throughout our nation.

Our package is intended to end the abuses which have plagued HUD programs and to regain the confidence of the American people. That is essential if we are to get back to the basic mission of HUD, which is to provide affordable housing opportunities for all Americans.

Mr. Chairman, our reforms are systemic and they involve improving checks and balances and accountability. But HUD is more than program rules and regulations. It is people, and the

reforms we are proposing will let the thousands of hard-working and dedicated men and women at HUD get back to doing, on a full time basis, the job of delivering assistance fairly and responsibly to those who seek housing opportunity and the opportunity for a better life.

In closing, Mr. Chairman, let me stress one more time how critical I consider these reforms to be. I ask your cooperation in considering these proposals on an urgent basis. Once that is done, we can go beyond reform and focus on the substance of housing issues.

Statement of Rep. Marge Roukema
October 12, 1989
Subcommittee Hearing with the Hon. Jack Kemp

Mr. Chairman, thank you for calling this hearing so promptly, and my thanks also to Secretary Kemp for agreeing so quickly to meet with us, especially since I know how pressing his schedule is.

The last several months have been difficult for all of us who are concerned about housing as one abuse after another has come to light. These have been examined by this Subcommittee and others. My sense is that we are coming to the end of the investigative phase of the scandal. There are two more phases which follow.

First, there must be a thorough and vigorous investigation by HUD and the Justice Department into any possible criminal activities. I understand that this is occurring with many investigations now under way and a number of prosecutions which have already commenced. I can only encourage the Attorney General to make this a high priority and to continue to pursue this in an aggressive manner.

Second, this Subcommittee must consider essential legislative reforms, and provide a house cleaning, if you will. That is our responsibility, and that is why we are here today.

Several proposals have already been introduced in the Congress. The Senate has already approved legislation dealing with lobby disclosure. The Chairman of the Employment and Housing Subcommittee (Mr. Lantos) has also introduced such legislation. The Gentleman from New York (Mr. Schumer) has introduced a couple of bills. And I have introduced legislation of my own to reform programs and procedures at HUD.

As I said at the time I introduced my bill, this is one of many proposals, and I look forward to working with my colleagues, with the Secretary and his people to enact a comprehensive bill which will deal effectively with the potential for abuse and corruption. We need a bill that will be more than mere cosmetics, one that will be administratively sound but not unreasonably burdensome for the Department. I am confident that, working together, we can produce legislation that is faithful to our Constitutional responsibility to represent and protect the public trust.

Since the introduction of my bill, the Secretary has announced his reform proposals. It is an impressive package, and I commend him for it.

Mr. Chairman, at this time I would just like to say something about Secretary Kemp. No Cabinet Secretary ever inherited a bigger or more complex set of problems. This Secretary of HUD faced those problems squarely and brought them out into the open. Under the most difficult of circumstances, he has acted responsibly, as a true public servant in a non-partisan manner. Now he has brought us a package of recommendations which are serious and responsive, and I look forward to today's discussion of the proposals.

I was particularly pleased to see the following recommendations from the Secretary: mandatory disclosure of consultant activities, strengthening the authority of the Inspector General, and creation of a Chief Financial Officer at HUD. All of these were major provisions in the bill which I had introduced, so, naturally, I was encouraged to see them in the Department's package.

In closing, Mr. Chairman, I would just like to reiterate my desire to work with you and with the Secretary to produce a reform bill as quickly as possible. The Secretary helps us enormously along that road with his proposals and by appearing here today. Thank you, Mr. Chairman.

HENRY B. GONZALEZ, TEXAS.

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U.S. HOUSE OF REPRESENTATIVES

SUBCOMMITTEE ON HOUSING AND COMMUNITY
DEVELOPMENT

OF THE

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

ONE HUNDRED FIRST CONGRESS

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October 5, 1989

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Honorable Tom Lantos
Chairman, Subcommittee on
Employment and Housing
Committee on Government Operations
U. S. House of Representatives
B349A Rayburn House Office Building
Washington, D.C. 20515


Dear Tom:

Enclosed for your consideration is the HUD Inspector General's report and audit of the Section 8 Project-Based Certificate Program completed at my request pursuant to my June 24, 1988, letter to the Inspector General. Here again the Inspector General has found that the Reagan/Pierce/HUD has engaged in the same type of misuse of an important HUD program that was found to be the case in his earlier report on the Section 8 Moderate Rehabilitation Program.

As you know, on Tuesday, October 3, Secretary Kemp announced a series of actions that he intends to take to clean up or as he states it, "clear the decks" at HUD. Many of his recommendations will involve statutory changes and will require action by my Subcommittee and the full Committee to give Secretary Kemp the tools he needs to clean up the Department.

As the Committee of legislative jurisdiction, my Committee will hear from Secretary Kemp on his justifications for the legislative changes that he believes necessary to assist him in dealing with these scandals. I would strongly urge you to continue your superb investigative efforts that will define the extent of the swamp in which the Pierce/HUD regime has left the Department. We on the legislative Committee will consider the legislative changes to repair the disaster areas in which HUD finds itself. With the Government Operations and Banking Committees working together, I believe that we can have HUD back serving the public interests instead of private interests.

Sincerely,


Henry B. Gonzalez
Chairman

Enc.

GM:jr

**REVIEW OF SECTION 8 EXISTING
CERTIFICATE PROGRAM FUND ALLOCATIONS**

FISCAL YEARS 1988 AND 1989

90-TS-203-0001

October 3, 1989



| |
|-------------------|
| Issue Date |
| October 3, 1989 |
| Audit Case Number |
| 90-TS-203-0001 |

TO: C. Austin Pitts, Assistant Secretary for Housing -
Federal Housing Commissioner, H

FROM: *Chris Greer*
Chris Greer, Assistant Inspector General for Audit, 2A

SUBJECT: Review of Section 8 Existing Certificate Program Fund
Allocations - Fiscal Years 1988 and 1989

In response to a request from Henry B. Gonzalez, Chairman of the House Subcommittee on Housing and Community Development, we reviewed the fund allocation process for the Section 8 Existing Certificate program for Fiscal Years (FY) 1988 and 1989. The primary purpose of the review was to determine the basis for funding allocations and to ascertain the possible impact on the implementation of the Project Based Assistance (PBA) component of the Section 8 Program. Our review encompassed the funding decisions made through December, 1988.

We concluded that the Headquarters Reserve funding allocation process lacked accountability and was not adequately documented. Consequently, we were unable to determine whether the PHAs selected were awarded Certificates strictly on merit or because of influence by Headquarters and Regional Office officials. For example, certain Regional Administrators advised that HUD Headquarters officials and staff influenced their requests for Headquarters Reserve funding and in some cases suggested how to use Fair Share allocations for specific PHAs.

We made five recommendations to upgrade the administrative and management controls governing the funding allocation process. On May 17, 1989, the General Deputy Assistant Secretary agreed to implement the draft report recommendations and improve the funding allocation process by issuing written instructions to PHAs and HUD Field Offices, establishing a standardized rating system for Headquarters Reserve funding allocations and providing Field Offices the ability to allocate funds in reasonable ways consistent with regulatory and statutory provisions and sound administrative practices. As a result, none of the remaining unallocated FY 1989 Certificates will be funded through Headquarters Reserve.

Within 60 days, please furnish this office, for each recommendation cited in the report, a status report on: (1) the clearance action taken; (2) the proposed clearance action and the date to be completed; or (3) why action is not considered necessary. Also, please furnish us copies of any correspondence or directives issued because of this report.

Should your staff have any questions, please have them contact Chris Greer, Assistant Inspector General for Audit at 755-6364.

EXECUTIVE SUMMARY

We reviewed the allocation process for Section 8 Existing Certificates for FY 1988 and 1989. Our review encompassed all funding decisions made through December, 1988. The review was initiated in response to a request from Henry B. Gonzales, Chairman of the House Subcommittee on Housing and Community Development. We focused attention on the process used to allocate funds and on the impact the fund allocations had on a Public Housing Authority's (PHA) ability to implement the Project Based Assistance (PBA) component of the Section 8 Program.

Specific concerns raised by Chairman Gonzales were that HUD is allocating Section 8 Existing Certificates on the basis of inside information, favoritism, and political bias. His concern is that meager Federal housing assistance funds be allocated on the basis of local need for housing, not on the private commitment of certain developers and housing authorities may have received from HUD officials outside the legitimate procurement process. Public Housing Authorities have been approached by developers who claim they have an inside track to an allocation of Section 8 Existing Certificates if the PHA will be willing to work with that particular developer in exercising the discretionary project-based approach permitted by the 1987 Act.

We concluded that the Headquarters Reserve funding allocation process lacked accountability and was not adequately documented. There was no criteria established to rate and rank PHA requests received for funding, or documentation supporting the selection of one PHA over another. Moreover, the availability of Headquarters Reserve funding allocations was not formally advertised. Those PHAs who knew the process of sending a request directly to Headquarters received a distinct advantage over other PHAs not knowledgeable of the process. All Regional Administrators provided a recommended list of PHAs for Headquarters Reserve funding allocations. However, five Regional Administrators advised us that the decision to include many of the specific PHAs was influenced by Headquarters inquiries. Seven funding decisions were not fully documented to show compliance with HUD Regulations (24 CFR 791.403) which describe six specific types of uses for Headquarters Reserve funds.

Generally the fair share allocations were completed in an equitable manner in accord with program requirements and local needs. However, there were indicators that Headquarters officials/staff contacted Regional Offices and suggested that specific PHAs receive fund allocations. This occurred at two Regions.

Our reviews at PHAs regarding the intended use for the funding allocations showed that some PHAs had specific projects targeted for Project Based Assistance (PBA). In several cases, PHAs were

approached by developers and/or former HUD officials (prior to the awarding of the funding allocations) regarding the potential use of Certificate allocations as PBA. Headquarter's officials advised that it is normal for developers to contact PHAs. Nevertheless, we believe the informal process used created perception and interpretation problems as to why certain PHAs were funded.

We provided five specific recommendations to overcome the current management control weaknesses. Policies and procedures should be adopted to upgrade accountability and documentation requirements. Clear guidance needs to be developed and communicated to appropriate staff regarding the proper roles that HUD staff and PHA staff should play in the funding allocation process.

We provided our draft report to the General Deputy Assistant Secretary for Housing on April 20, 1989. Prompt action was initiated and on May 17, 1989, he fully responded to our draft report and recommendations. In the response he agreed to improve the funding allocation process by implementing the five recommendations. His response also indicated that certain factual errors may exist in the draft report. Accordingly, we provided the draft report to the former Assistant Secretary and on June 13, 1989, he provided a written response. Based on the response, the draft report was revised to include new information which was not provided to us during our review. On August 14, 1989, a meeting was held with the former Assistant Secretary to discuss the revised draft report. We have included pertinent comments of HUD officials and the former Assistant Secretary as we deem appropriate.

**REVIEW OF THE SECTION 8 EXISTING
CERTIFICATE PROGRAM FUND ALLOCATIONS-
FISCAL YEARS 1988 AND 1989**

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INTRODUCTION

A. BACKGROUND

Fair-Share Allocations

Section 213(d) of the Housing and Community Development Act of 1974 provides for the fair-sharing of contract and budget authority for housing assistance. Consequently, unless specifically waived each year by annual appropriations acts, HUD fair shares assisted housing funding authority to Regional Administrators or directly to Field Office Managers who in turn allocate such authority within their jurisdictions. For FY 1988, Congress approved a waiver to Section 213(d) of the Act, making the Regulations 791.403 (b) non-effective. In FY 1989, compliance with the Regulations was not waived.

The fair share calculations are performed by the Office of the Assistant Secretary for Policy Development and Research (PD&R). That Office determines the relative need for lower-income housing assistance in each HUD Field Office jurisdiction. To the extent practicable, this determination is based on the most recent national census data available relating to population, poverty, housing overcrowding, housing vacancies, amount of substandard housing and other relevant measurable conditions. PD&R then develops a separate housing needs percentage for both metropolitan and nonmetropolitan portions of each Field Office jurisdiction, adjusted to reflect the relative cost of providing housing among the Field Office jurisdictions.

The Office of the Assistant Secretary for Housing - FHA Commissioner then determines the amount of contract and budget authority that is to be allocated. This determination is based on any unreserved contract and budget authority available from prior fiscal years, as well as newly appropriated authority. Prior to FY 1989, HUD was required to allocate, on a nationwide basis, at least 20 percent, but not more than 25 percent of the contract authority available during the fiscal year for use in nonmetropolitan areas. This allocation is set forth in an annual Fund Assignment Plan.

Headquarters Reserve Allocations

Pursuant to Section 213(d)(4) of the Housing and Community Development Act of 1974, the Secretary may retain up to 15 percent of available contract authority for assisted housing for subsequent allocation to specific areas and communities. This is referred to as the Secretary's discretionary fund or the Headquarters Reserve. These discretionary or reserve funds may be used only for the following:

- 1) Unforseeable housing needs, especially those brought on by natural disasters or special relocation requirements;
- 2) Support for the needs of the handicapped or for minority enterprise;
- 3) Providing for assisted housing as a result of the settlement of litigation
- 4) Small research and demonstration projects;
- 5) Lower-income housing needs described in Housing Assistance Plans, including activities carried out under an areawide housing plan;
- 6) Innovative housing programs or alternative methods for meeting lower-income housing needs approved by the appropriate Assistant Secretary, including assistance for infrastructure in connection with the Indian Housing Program.

The 15 percent Headquarters Reserve need not be applied to each particular program comprising the total authority available for housing assistance. Rather, it may be based on the total contract authority available for housing assistance (i.e. Section 8, Section 202, PHA development, etc). However, it should be noted that the balance of available authority, after computation of the Headquarters Reserve, is not all earmarked for fair-sharing. Rather, a portion of the authority is set aside for such items as contract amendments, property disposition, loan management, voucher renewals, PH demolitions, etc.

The Section 8 Existing Certificates for Fiscal Years 1988 and 1989 were:

| <u>CERTIFICATES</u> | <u>FY 1988</u> | <u>FY 1989</u> |
|----------------------|----------------|----------------|
| Fair Share | 7800 | 7119 |
| Headquarters Reserve | 1459 | 9632 |
| Other | <u>646</u> | <u>1583</u> |
| Total | <u>9905</u> | <u>18,334</u> |

On December 28, 1988, the FY 1989 fund assignments for 11,188 of the 18,334 units were made. The Regional Offices were allocated 4,769 units from the Headquarters Reserve and 6,419 units from Fair Share.

Project Based Assistance

Section 8(d)(2) of the United States Housing Act of 1937, as amended by Section 148 of the Housing and Community Development Act of 1987 approved February 5, 1988, concerns the attachment of Section 8 Assistance to existing structures and newly constructed structures. The amendment specifically requires the Secretary to use authority previously provided by law to allow a PHA, at its sole discretion, to implement Project Based Assistance (PBA). The PBA program provides that a PHA may choose to attach up to 15 percent of its Section 8 Existing Certificate universe to specific projects.

On January 5, 1989, the former Assistant Secretary for Housing issued a memorandum to all Regional Administrators and Field Office Managers to clarify the Department's position regarding Section 8 Certificate allocations. The memorandum provided:

"I want to stress that no new funds are being provided expressly for the project-based component of the Certificate Program"

"PHAs must be clearly advised that there is no separate funding for the Project Based Certificate Program and requests for such funding to Headquarters or Field Offices are inappropriate."

Specific requirements for implementing and administering the PBA are contained in the Section 8 Certificate Program - PBA Interim Rule published on January 4, 1989.

B. OBJECTIVES AND SCOPE

The review objectives were to: determine whether HUD allocated Section 8 Certificates in conformance with established regulations and procedures, and, evaluate the impact fund allocations had on the Public Housing Authorities' ability to implement the new PBA component of the Section 8 Program.

Our review consisted of interviews with Headquarters Officials, Regional Administrators, and Field Office Managers and staff, and PHA Executive Directors; a review of program regulations; and an analysis of supporting documents for the Section 8 Certificate allocations for FYs 1988 and 1989. The review was performed between February and August 1989 and covered funding decisions through December, 1988. We conducted the survey using generally accepted government auditing standards.

Results of Survey

A. Finding and Recommendations

Finding 1 - Need to Improve The Accountability and Documentation For Funding Allocations

The Headquarters Reserve funding allocation process lacked accountability and was not adequately documented. There was no criteria established to rate and rank PHA requests received for funding, or documentation supporting the selection of one PHA over another. Moreover, the availability of Headquarters Reserve funding allocations units was not formally advertised. Those PHAs who knew the process of sending a request directly to Headquarters received a distinct advantage over other PHAs not knowledgeable of the process. All Regional Administrators provided a recommended list of PHAs for Headquarters Reserve funding allocations. However, five Regional Administrators advised us that the decision to include many of the specific PHAs was influenced by Headquarters inquiries. Seven funding decisions were not fully documented to show compliance with HUD Regulations (24 CFR 791.403) which describe six specific types of uses for Headquarters Reserve funds.

Generally the fair share allocations were completed in an equitable manner in accord with program requirements and local needs. However, there were indicators that Headquarters officials/staff contacted Regional Offices and suggested that specific PHAs receive fund allocations. This occurred at two Regions.

The following two sections discuss general and specific problems concerning funding selections from the Headquarters Reserve and Fair Share allocations.

a. Headquarters Reserve

The regulations for Certificates governing the Headquarters Reserve allocation process are in 24 CFR Section 791.403(b) (refer to Background Section, page 1). Based on the regulations the Assistant Secretary for Housing is authorized to allocate up to 15 percent of contract and budget authority in any fiscal year on a discretionary basis. The Headquarters Reserve funding allocation process for FY 1988 and FY 1989 were not formally announced via memoranda or other instructions. Details concerning the amounts of funding available or the methods and criteria for making funding decisions were not communicated in any systematic fashion.

We interviewed the former Assistant Secretary and Headquarters staff responsible for the Section 8 Certificate program and staff responsible for assembling data in support of funding decisions. Additionally, we interviewed the Regional Administrators and Regional Housing staff at the 10 Regional Offices. We contacted the Executive Directors or staff at the PHAs receiving Headquarters Reserve funding allocations during FY 1988 (10 PHAs) and FY 1989 (46 PHAs).

For the 10 PHAs funded in FY 1988 the only documentation provided to support the funding decisions were PHA requests to Headquarters. Our analysis of the request letters disclosed that the basis for requesting the Certificates was a shortage of housing. We believe that most PHAs have similar housing shortages as these ten PHAs. The former Assistant Secretary advised that his decisions were based on a housing need or a litigation settlement.

Headquarters provided us with a document outlining the Funding Decision and Chronology process followed in selecting PHAs funded from the FY 89 Headquarters Reserve. Our review of the process for allocating Headquarters Reserve Certificates shows that it did not meet the requirements for accountability because of a lack of documentation.

HUD allocated a total of \$279 million of budget authority from the Headquarters Reserve for FY 1988 and FY 1989. The funding plan prepared in October 1988 by the Office of Housing for FY 1989 provided more than 52 percent of the total Section 8 Existing Certificates to be allocated from the Headquarters Reserve. We believe that a commitment of Federal funds of this magnitude should require more than an informal process, i.e., documentation, criteria, and rationale for the decisions.

A legal opinion was requested by the former Assistant Secretary regarding the distribution of Headquarters Reserve and compliance with Section 213(d) requirements for FY 1989 allocations. On November 8, 1988, the Assistant General Counsel, Assisted Housing Division, provided an opinion on the use of Certificates from the Headquarters Reserve. The opinion states in part:

"Certificates or other USH Act funds in the Reserve may only be used for one of six purposes specified in the statute and program regulation (section 791.403(B)). There are no other program restrictions on the specific purposes for which the Reserve Certificate funds may be used (within the universe of uses allowed under the statute and program regulations). There are also no required procedures for allocation of the funds as between authorized uses of Reserve funds, or for geographical distribution of the funds. The ultimate determination on the purposes for which the funds will be used rests in the discretion of the Assistant Secretary,

so long as there is a valid administrative basis for the choice." (underscoring provided)

. . . .

"To support your decision on use of Certificate or other Reserve funds, the informal administrative record should be sufficient to show that the selected use is within one of the six statutory purposes, and that the decision to use the funds for the selected use is reasonable (not 'arbitrary and capricious')."

The opinion did not require a process for documentation and accountability. However, we believe the opinion provided sufficient guidance that the decision-making process should not be arbitrary and capricious, hence a means for selection should exist.

Headquarters officials advised that the Regional Offices were not requested to include any PHA or "specific projects" on their list of recommendations for the FY 1989 allocations. Regional Offices were requested to give input or recommendations, either negative or positive, as to each PHA being considered.

From November 3 to November 17, 1988, Headquarters Staff Assistants began calling the Regional Administrators (RAs) to seek field input on requests for funding from the Headquarters Reserve. Using this process of calling each Regional Administrator created perception and interpretation problems. Five Regions advised they considered these requests to mean that specific PHAs were already approved for funding and they were to provide support for the decision.

A former Staff Assistant to the former Assistant Secretary advised that in late October or early November, 1988, the former Assistant Secretary provided a stack of PHA requests, with instructions to contact each Regional Office in an attempt to determine which PHAs were eligible and deserving of funding. The former Assistant Secretary advised that the number of PHAs considered for FY 1989 funding was derived from the Regional Administrator's recommended lists and PHA requests. There was a total of 94 PHAs considered for the FY 1989 Headquarters Reserve. We believe there are a greater number of PHAs with the same type of needs as the 94 PHAs considered.

The Regional Administrators' lists of recommended PHAs to the Assistant Secretary were received within a few days of the request (November 3, 1988) which raises questions on the completeness and fairness of the process. In addition, most Regional Administrator's responses stated that the PHAs met criteria number 5, lower-income housing needs described in HAPs. Our analysis of the 46 PHAs funded in FY 1989 shows that 44 PHAs

were on the Recommended List provided by Regional Administrators. There was some type of documentation provided by the Regional Administrators to indicate that 39 PHAs met one of the six regulatory criteria:

| <u>Criterion</u> | <u># of PHAs</u> |
|------------------|------------------|
| 1 | 2 |
| 2 | 4 |
| 5 | 33 |
| | <u>39</u> |

Seven PHAs lacked documentation showing which regulatory criteria was met. The former Assistant Secretary and Headquarters Officials advised that the PHAs selected met one of the six regulatory criteria and the purpose of the Headquarter's staff calls to Regional Administrators was to assure one of the six criteria was met. However, the criteria is very general in nature, such as, does the community have a HAP or an areawide housing assistance plan. By following this process, Headquarters was able to state that the selections met the regulations. The problem with this informal process is that it lacks accountability and documentation. We do not believe that Congress intended total discretion without accountability for the use of the Headquarters Reserve.

Five Regional Administrators provided their interpretations of the informal process used to allocate Headquarters Reserve Certificates:

Region I

The former Regional Administrator advised that he signed the letter based on a request by the Region's Director of Housing and he had no other information as to why the PHAs would be funded. The Director of Housing advised that Headquarters needed Region I's endorsement of the PHAs. He advised that a former staff assistant to the former Assistant Secretary called the Region and identified three of the four PHAs to be included in the the Region's request letter.

Region IV

The Regional Administrator advised that the former Assistant Secretary's Staff Assistant telephoned and told the Region that before certain PHAs could be funded Headquarters needed a letter from Region IV indicating that the PHAs should be funded. The Staff Assistant did not say that these PHAs

would be funded, but implied that they would be funded. These PHAs were selected in Headquarters without any input from the Region or Field Offices other than the telephone request for a justification for funding the PHAs. The Regional Administrator stated that he supports the funding of these PHAs because he would support any PHA in Region IV getting more Section 8 Certificates.

Region VI

The Regional Administrator advised that on numerous occasions during the latter part of 1988 the former Assistant Secretary's staff contacted the Region relative to the selection of PHAs for the Section 8 Certificate Program Headquarters Reserve fund allocation process. The calls from Headquarters involved the selection of five (5) PHAs. The calls were initiated by the Headquarters staff and tended to involve questioning as to the strengths and weaknesses of each PHA as a candidate for Section 8 certificates. Consequently Headquarters would recommend PHAs for Section 8 certificates and contact the Region to confirm that the particular PHA had the demonstrated capacity to successfully administer the additional units. The Region was asked to verify whether the need for such units existed in the community. The Regional Administrator recommended the 5 PHAs.

Region VIII

The former Regional Administrator advised that he received a call from a Staff Assistant to the former Assistant Secretary on November 4, 1988. The Staff Assistant advised that Section 8 certificates were being allocated from Headquarters to the North Dakota Housing Authority (NDHA) and the Ogden Housing Authority. After conversation with the Staff Assistant, the Regional Administrator met with the Housing Programs Branch Chief and the Director of Public Housing to discuss the merits of NDHA and Ogden Housing Authority. Both felt the housing authorities were deserving of the certificates and on that same day the memorandum was sent to Headquarters. It should be noted that Headquarters did not select the North Dakota Housing Authority for funding.

Region IX

The Regional Administrator advised that he had a series of conversations with the former Assistant Secretary for Housing and with Staff Assistants concerning the allocations

of Section 8 certificates during the 1988 and 1989 allocations. The substance of the telephone calls was to ask the Region to prepare letters for specified PHAs identifying a need existed and HAP compliance (the particular PHA was always specified and no mention of specific projects occurred). It was the Assistant Secretary who determined the majority of Public Housing Authorities that were allocated units.

* * * * *

The former Assistant Secretary advised it is clear from the administrative record that each Regional Administrator had the opportunity to agree or disagree on any given PHA which had written for consideration, and in fact several Regional Administrators supplemented the list by adding other PHAs. We believe that without adequate documentation, there is no way to evaluate the reasonableness of these decisions.

Appendix A summarizes the survey indicators associated with PHAs selected for funding allocations from the Headquarters Reserve. For example, five Regional Administrators advised that Staff Assistants to the former Assistant Secretary called and suggested that the Regional Administrators write memorandums to Headquarters requesting funding allocations for specific PHAs. At least 17 of the 46 PHAs selected in FY 1989 were funded in this manner. We believe that most PHAs are unaware of this funding availability or of the possibility of requesting funding directly from Headquarters.

The following examples demonstrate the perception and interpretation problems created by the informal process followed in allocating Section 8 Certificates from the Headquarters Reserve Fund during Fiscal Years 1988 and 1989.

PHA - Massachusetts Executive Office of Communities and Development (EOCD) (FY 1988 Allocation)

In May 1988, EOCD submitted a "generic application" to HUD for the Fiscal Year 1988 Section 8 certificate allocation. EOCD requested 802 certificates.

A HUD representative called EOCD approximately the last week of September 1988, and asked that EOCD submit an amendment to its May 1988 Greater Boston application. EOCD understood at the time of this request that 125 PHA certificates were designated by HUD for the Castle Square project. EOCD was surprised to receive telephone requests from the HUD representative, since EOCD usually receives a region-wide allocation of certificates rather than site specific.

In February of 1988 the Winn Management Company (WMC) signed a purchase and sales agreement with the Drucker Company (DC), to purchase the property known as Castle Square. The reason DC was selling the property was because the twenty year "expiring use contract" with HUD had expired and DC did not wish to remain in the subsidized housing business.

WMC contacted the former Assistant Secretary to arrange a meeting to discuss the Castle Square project. During this meeting WMC presented to the Assistant Secretary the possibility of Castle Square receiving 500 units of Section 8 Moderate Rehabilitation funding. Ultimately the former Assistant Secretary rejected this proposal and approximately ten additional meetings occurred with several Headquarters Officials between January 1988, and September 30, 1988.

On July 18, 1988, the former Assistant Secretary requested the former Under Secretary to replace him in the ongoing negotiations on the Castle Square Project. The former Assistant Secretary recused himself in all matters arising from and pertaining to this developer.

We are concerned about the decision to fund this PHA, since the PHA's original request was a generic application and not project specific. The former Assistant Secretary and other HUD Officials had several meetings on this specific project with the developer. We believe the decision was to fund a specific project and not the overall needs of the PHA.

Bayamon, Puerto Rico (FY 1988 and FY 1989 Allocation)

On November 30, 1987, the Municipality of Bayamon requested Headquarters to provide 350 Section 8 Certificates in order to meet a portion of their immediate needs. The Mayor of the Municipality of Bayamon stated that they suffer from an urgent and continuous need for housing and, with the help of the Section 8 Certificates program, they have been able to assist many low income families. On February 25, 1988, HUD allocated 350 Certificates to the Bayamon Housing Authority.

On September 26, 1988, the Acting Regional Administrator rescinded the 350 Certificate allocation and reallocated 100 Certificates to Bayamon. On December 28, 1988, an additional 200 FY 1989 Certificates were allocated from the Headquarters Reserve.

The Region II Director of Program Support for Housing advised that since July 1988, he participated in discussions about the 350 Housing Certificates which Headquarters assigned to Bayamon, Puerto Rico. The substance of the discussion was "Why were so many units going in one fell swoop to Bayamon?" However, they

were after the allocations, not before. He was not aware of any request for special funding for Bayamon. He believes that the Bayamon funding was unusual. In January 1989, when the Revised Fiscal Year 1989 Fund Assignment memo was received, he again observed funds being allocated for Bayamon from Headquarters reserve.

The Regional Director of Program Support statements show the problems HUD has created by following an informal process without accountability and documentation. The rationale for the decision creates the appearance of preferential treatment. The former Assistant Secretary advised that all of the documentation originating from Bayamon should be substantive and valid reasons for the selection. We disagree. The decision to fund the PHA is not clearly supported by documentation because the PHA letter of November 30, 1987, only states they have an urgent need of housing.

Yuma, Arizona (FY 1988 Allocation)

On July 22, 1988, the PHA requested 100 units of Section 8 Certificates. The PHA letter indicated that as of May 1, 1988, there were 537 households on the waiting list for the Section 8 Existing Housing and Housing Voucher Programs and that the application is in compliance with the Housing Assistance Plan most recently approved by HUD. The Area Office recommended a low funding priority to Yuma because the HUD Regional Economist's review of the City's application concluded that the City has been over funded relative to its fair share of rental subsidy.

The Executive Director of the Housing Authority of the City of Yuma advised that he learned that the best way to apply for additional Certificates was to write directly to the HUD Central Office. He requested 100 Existing Housing Section 8 Certificates. The former Assistant Secretary wrote back and informed him that the PHA would not be receiving any of the 100 new certificates requested.

During October 1988, he received a number of telephone calls from developers advising that the PHA had been funded for additional Section 8 certificates. Approximately in the same period he received telephone calls from two former HUD officials from Colorado. They said that they understood that the PHA had been funded for additional Section 8 certificates and asked whether the housing authority was going to devote any certificates to PBA projects.

After receiving telephone calls he called the Phoenix HUD office and asked whether they actually had been allocated some additional Section 8 Certificates. The Phoenix Office confirmed that the PHA had been funded for the 100 additional units. The

Executive Director advised that the developers who telephoned were aware of the additional certificates to the PHA even before the Phoenix HUD office knew of the decision.

The allocation funded approximately 22 percent of the PHA's needs based on the request dated July 22, 1988. We believe other PHAs have greater needs than this PHA and that the rationale for the decision is questionable. Further, questions are raised concerning the informal process because developers and former HUD Officials were aware of the funding allocation even before the PHA.

PHA - Jefferson Parish, LA (FY 1988 and FY 1989 Allocations)

Funding allocations from the Headquarters Reserve were provided to Jefferson Parish for both FY 1988 and 1989. Headquarters Officials advised that they were unable to locate written documentation for the allocation of 150 Certificates for FY 88.

On December 28, 1988, 200 Certificates were provided to Jefferson Parish Housing Authority. The Headquarters staff had requested the Regional Office to request funding for this PHA on the Regional Administrator's list.

The former Assistant Secretary advised he had several meetings with the President of Jefferson Parish and Parish Council. He made at least three separate visits to the area. The Area Manager was also strongly supportive of the Jefferson Parish applications and the former Assistant Secretary understood the generic and not the specific needs of the PHA.

The Housing Program Administrator of Jefferson Parish advised that one developer was trying to "bulldoze" his way through the Jefferson Parish Housing Authority and Community Development Office trying to obtain any new Section 8 Certificates awarded. This developer always seemed to have information pertaining to the Section 8 Certificates prior to anyone else. The developer seemed to have the ability and the contacts within HUD to get the job done. It also appeared that the developer had someone within HUD who was supplying him with information.

The Administrator advised that the developer already had a financial commitment to provide the funding to rehabilitate the Scottsdale Apartments if he was able to obtain a commitment of Section 8 Certificates from the PHA. However, the developer never submitted a specific request or proposal to the PHA asking for a certain number of Project Based Section 8 Certificates for the project and no decision was made by the PHA to allocate any Project Based Section 8 Certificates to facilitate the rehabilitation of the Scottsdale Apartments.

Due to a lack of documentation supporting the decision, the rationale for funding Jefferson Parish in both FY 88 and FY 89 is questionable and points to the need for a formal process with accountability and documentation.

PHA - Arvada Housing Authority CO (FY 1988 Allocation)

On November 30, 1987 the PHA made an official request for 80 one-bedroom and 20 three-bedroom Section 8 Certificates from the Secretary's Headquarters Reserve. The request stated that the need for Section 8 assistance in Arvada is great. In addition, the current Housing Assistance Plan (HAP) for the City of Arvada approved by HUD estimated 437 elderly and 1,568 small family and 137 large family households needed rental assistance.

On February 25, 1988, the PHA was funded with 100 Section 8 Certificates. The PHA Executive Director advised that he had a conversation with a former HUD Under Secretary regarding the Section 8 Certificate Program. The former HUD official told him that he should apply for certificates from the Secretary's Headquarters Reserve fund. He never knew such a Reserve existed. In the past, AHA has only applied for certificates in response to advertisements for funding. The former HUD official explained to him what the Reserve fund was. A few days later he received a "model" draft letter for the Regional Administrator requesting Section 8 Certificates. On November 30, 1987, AHA transferred the letter onto their stationery and mailed one copy to the Regional Administrator and one copy to Headquarters. HUD notified AHA approximately two months later that the 100 certificates were provided.

We believe that the knowledge of a former HUD Official as to the Headquarters Reserve process provided a distinct advantage to this PHA. In addition, without adequate documentation the decision to fund the PHA is questionable.

Department of Housing - Connecticut (FY 1989 Allocation)

The State of Connecticut Department of Housing received 150 Section 8 Certificates specifically designated for the City of Norwich. The Connecticut Housing Finance Authority submitted a request on behalf of the Department of Housing for Project Based Certificates in order to fund the American Finishing Mill (also known as the Bleachery) in Norwich.

The HUD Field Office Manager believed that these units were allocated as Project Based Assistance in support of the American Finishing Mill located in Norwich. He further believed that Headquarters' decision to allocate these units was based on the history of the project and the developer's attempts to obtain

Moderate Rehabilitation funding for this project from Headquarters in the past. When the allocation was made specifically for Norwich, there was no question among the Field Office staff that these Certificates were allocated for this project.

The State of Connecticut Department of Housing (CDOH) advised that on March 2, 1989 CDOH learned for the first time that a specific developer was developing a project known as the Bleachery in Norwich, Connecticut. CDOH also learned that the Bleachery was to receive 150 Project Based Assistance (PBA) certificates for use in this project. In June 1989, CDOH called the developer for the Bleachery Project and the developer told the CDOH that he got these Section 8 certificates. However, CDOH informed the developer that the 150 Section 8 certificates would be placed into CDOH's regular Section 8 existing program, unless otherwise directed.

We believe the statements show that the decision was to fund a specific project. HUD needs to develop a process which provides for the rationale for the funding decisions from the Headquarters Reserve.

b. Fair Share

Our review indicates that generally the Fair Share allocations were completed in an equitable manner in accord with program requirements and local needs. However, there were indicators that Headquarters Officials/staff contacted Regional Offices and suggested that specific PHAs receive fund allocations at the two Regions discussed below.

Region IV

The Regional Administrator advised that in early 1988 he decided to "Fair Share" the initial allocation of Section 8 Certificates to the Field Offices. He received a telephone call from the Executive Assistant to the former Assistant Secretary. She seemed concerned that the Region had fair shared the Section 8 Certificates to the Field Offices. The Executive Assistant suggested pulling back the fair shared Section 8 Certificates that were sent to Field Offices.

The Executive Assistant on numerous occasions contacted the Regional Administrator, suggesting Headquarter's interest in several PHAs being allocated certificates. She would say something like, "You should think about funding this or that PHA." She never directed the Regional Administrator to fund any PHA, but she made him aware that Headquarters would like to allocate certain units to particular PHAs and the

Regional Administrator tried to respond to what he thought Headquarters wanted. She did not tell him where the Headquarter's interest came from, such as the PHA, a developer, or HUD Official.

The Regional Administrator believes the Executive Assistant told him that Headquarters had an interest in DeKalb County Housing Authority (DCHA) being funded. DCHA did receive the entire amount of Section 8 Certificates allocated to the Georgia area.

He also received one telephone call from the Executive Assistant concerning a project in Rome, Georgia. She asked him if the project could be funded. The Georgia Residential Finance Authority (GRFA) administers the Section 8 for the Rome area.

The Regional Administrator was aware of an interest in the South Carolina State Housing Authority (SCSHA), by a developer who wanted to develop a 112 unit project in West Columbia, South Carolina. The Regional Administrator did not have any direct contact with the developer regarding the West Columbia project, but he did speak with his consultant. The consultant told the Regional Administrator that they were interested in developing a project with Mod Rehab funds. The consultant expressed an interest in participating in the PBA program. The Regional Administrator told the consultant that he would have to apply through a PHA that had a lot of certificates, and that the PHA would make the final decision whether to use the Section 8 Certificates as PBA Certificates. The Executive Assistant later told the Regional Administrator that Headquarters was aware that the developers had expressed an interest in SCSHA. She suggested that he ought to think about funding SCSHA, because they had a large amount of certificates and could do Project Based Assistance and that they were on the Mod Rehab list as well as the Project Based list. When he made the final selections, he increased the number of certificates by 150 because someone asked him to. He does not recall specifically who, but believes it was the Executive Assistant. The Regional Administrator did this partially because he knew that Headquarters wanted the SCSHA to receive the certificates. The Regional Administrator feels that the SCSHA should have been funded because he believes that they had originally applied for Mod Rehab funds and had not received them.

The former Assistant Secretary disagrees with the Region IV, Regional Administrator's statements that Headquarters suggested any of these PHAs for funding.

Region I

The Regional Director of Housing advised that he received a conference call from the former Assistant Secretary and a Congressman. They discussed the need for Certificates pertaining to the negotiated sale of the North Canal Apartments. The Congressman inquired if HUD could provide some sort of subsidy for 65 units. The former Assistant Secretary asked if the Region could provide 65 Certificates out of the Fair Share Section 8 allocation. The Regional Director of Housing agreed with this allocation. On September 30, 1988, the Region sent a letter to EOCB allocating 65 Certificates specifically as PBA for the North Canal Apartments. In response to the Inspector General's written questions concerning the project specific designation, the former Assistant Secretary advised that the Region misunderstood how PBA operates. The Region subsequently rescinded the project specific September 30, 1988 letter; however, the Certificates remained with EOCB.

* * * *

Former Assistant Secretary Comments

In response to the draft report, the former Assistant Secretary advised that he did not violate any regulation in using discretion for the selected PHAs. The Office of Housing's ability to respond to requests from Senators and Members of Congress played an important role in the decision process. While the OIG may disagree with the Headquarters Reserve and Discretionary provision of the Section 791 regulations as well as the underlying Section 213(d) statute, nonetheless they reflect the goals and objectives of the National Housing Act as well as Congressional intent. It is the responsibility of the Assistant Secretary for Housing to implement them to meet special housing needs as outlined in the 791.403(b) regulation.

He believes that the objective of our audit was to change the concept of discretion allowed by Congress to the Assistant Secretary for Housing during the last 13 years for allocating Headquarters Reserve units by making the process one of a formula-driven, and almost a mechanical process. The former Assistant Secretary advised that for 12 of the last 13 years the process was beyond informal because there was no process at all. The former Assistant Secretary stated that he was the first Assistant Secretary for Housing to give Regional Administrators some input in the decision making process for the Headquarters Reserve and cannot understand why certain Regional Administrators were confused as to the process. The former Assistant Secretary is concerned that the report gives the impression that the

decision making process was made "off the wall" when the real question is the extent to which the Headquarters Reserve funding allocations should be documented. He advised that there was never a requirement on the Assistant Secretary to provide a rationale other than meeting one of the six regulatory criteria in which all the funded PHAs met.

OIG Comments

Because of the absence of clear written policy and guidelines, we believe that the process administered for the FY 1988 and FY 1989 Certificates created a widespread perception that certain PHAs were favored, thus impairing the program's integrity. Since all PHAs were not aware of the Headquarters Reserve Certificates process, there is little assurance that the limited amount of Certificates were provided to those PHAs having the greatest need. The former Assistant Secretary believes that he does not need to fund the PHA with the greatest needs. New procedures are needed. One alternative for overcoming the perception and accountability weaknesses is to place greater responsibility for input and/or decision making at the Regional Office level. A key consideration in the design of any new system should be the impact that the selection process has on the overall management control system.

Draft Report Recommendations and Auditee Comments

In our draft report we recommended that the General Deputy Assistant Secretary:

- 1A. Issue instructions on how Headquarters Reserve allocations will be made.
- 1B. Establish submission requirements and standards for rating and ranking PHAs for possible funding from the Headquarters Reserve to assure an open and objective process.
- 1C. Make public the methods of submission, ranking, and allocating Headquarters Reserve funding.
- 1D. Require full documentation at the Headquarters level supporting the rationale for funding Headquarters Reserve allocations.
- 1E. Reemphasize through written instructions that fair share allocations be made to locations based primarily on need and that PBA is to be accomplished solely at the PHA's option.

In response to the draft report the General Deputy Assistant Secretary agreed to issue written instructions to PHA and HUD Field Offices with respect to the process to be followed in requesting funds from the Headquarters Reserve. A standardized rating system will be established. The Field Office will send the PHA's letter and application and its recommendations (with appropriate documentation) to Headquarters. The Assistant Secretary will review the Field Office submission and, will only approve a PHA's request in full or in part if the Field Office recommendation is positive. This policy is not intended to limit the discretion of the Assistant Secretary to further Departmental priorities through the use of set-asides for which competitive procedures will be established through publication of Notifications of Fund Availability in the Federal Register. The PHA request and the Field Office analysis will serve as the basic documentation for the funding decision.

In summary, the General Deputy Assistant Secretary believes that although need is an important consideration, Field Offices should have the ability to allocate their funds in reasonable ways consistent with regulatory and statutory directions, and sound administrative practices. Headquarters will not direct the use of "fair share" funds, and additional units will only be provided out of the Headquarters Reserve pursuant to the process set forth in our response to Recommendations 1A-D. We will once again emphasize that is the PHA's decision, not HUD's whether or not to use the Project-Based assistance option. We intend to provide language to this effect to be included as part of every Field Office Notification of Application Approval letter. In addition, our instructions to the field concerning the process to be followed in requesting funds from the Headquarters Reserve will also provide similar language. We note that training of PHAs, which occurred subsequent to this audit, emphatically made this point as did my memorandum of May 8, 1989.

OIG Evaluation of Auditee Comments

The agreement to implement the Recommendations together with the actions taken adequately addresses our concerns. Accordingly, our final report contains no further recommendations. However, the recommendations in our draft report will be tracked through the Audits Management System until the promised actions are fully implemented.

B. COMPLIANCE AND INTERNAL CONTROLS**Compliance**

We selected and tested transactions and records to determine compliance with laws and regulations that prescribe Section 8 Certificate allocation requirements. The results of our tests indicate that for the items tested, HUD generally complied with these laws and regulations, except as described in the finding.

Internal Control

We reviewed the internal controls relating to the allocation of Section 8 Certificates from the Secretary's Headquarters Reserve. Specifically, we found that the controls were non-existent and need to be established regarding the allocation of Certificates from the Secretary's Headquarters Reserve.

SUMMARY OF HEADQUARTERS
RESERVE FUNDING SELECTIONS
FY 1988 AND FY 1989

| Region | Public Housing Authority | No of Units | Survey Indicators | | | | |
|--------|-------------------------------|-------------|-------------------|---|---|---|---|
| 1 | Massachusetts EOCD | 125 (1) | | | | | E |
| | Conn. Department of Housing | 150 | A | B | | D | E |
| | Maine SHA | 100 | A | B | | | |
| 2 | Bayamon | 350 (1) | | B | | | E |
| | Bayamon | 200 | | B | | | E |
| | Vega Baja | 25 | | B | | | |
| | Arecibo | 50 | | B | | | |
| | CRUV | 300 | | | | | |
| 3 | Washington County (Maryland) | 20 (1) | | | | | |
| | Pittsburgh | 207 | | B | | D | E |
| | Norfolk | 44 | | | | | |
| | Delaware SHA | 50 | | | | | |
| | Jackson County (W. Virginia) | 50 | | | | | |
| 4 | Georgia RFA | 118 (1) | | | | | |
| | Miami Beach | 220 (1) | | B | | | E |
| | Lexington-Fayette (Kentucky) | 32 | | | | | |
| | Pascagoula (Mississippi) | 150 | A | | | | |
| | Jacksonville | 184 | A | | | | |
| | Pinellas County (Florida) | 175 | A | B | | D | E |
| | Hillsborough County (Florida) | 150 | A | | | | |
| | Mobile | 70 | A | B | | | |
| 5 | Chicago | 175 | | B | | | |
| | Michigan SHDA | 200 | | B | | | |
| | Anderson (Indiana) | 50 | | | | | |
| 6 | Jefferson Parish (Louisiana) | 150 (1) | | | | | |
| | Jefferson Parish (Louisiana) | 200 | A | B | C | D | |
| | Bexar County (Texas) | 125 | A | | | | |
| | Beaumont | 50 | | | | | |
| | Austin | 100 | A | B | C | D | |
| | Oklahoma City | 100 | A | | | | |
| 7 | Davenport | 36 | | B | | | E |

SUMMARY OF HEADQUARTERS
RESERVE FUNDING SELECTIONS
FY 1988 AND FY 1989

| Region | Public Housing Authority | No of Units | Survey Indicators | | | | |
|--------|-----------------------------|----------------|-------------------|---|---|---|---|
| | | | | | | | |
| 8 | Arvada -- <i>Arvada</i> | 100 (1) | | B | C | D | |
| | Colorado HFA | 150 | | B | C | | |
| | Ogden | 30 | A | B | | | E |
| | Colo. Dept. of Institutions | 50 | | | | | |
| | South Dakota HFA | 75 | | B | C | D | |
| | Montana DOC | 50 | | | | | |
| | Wyoming CDA | 75 | | | | | |
| 9 | Los Angeles City | 151 (1) | | B | | | |
| | Los Angeles City | 200 | A | B | | | |
| | Santa Rosa | 125 (1) | | B | | D | |
| | Yuma | 100 (1) | | B | C | D | E |
| | Fresno | 50 | A | B | | | |
| | Garden Grove | 200 | A | B | | | |
| | Oakland | 50 | | | | | |
| | San Bernardino | 175 | A | B | | D | |
| | San Diego | 50 | A | B | | | |
| | Maricopa County (Arizona) | 150 | | B | C | D | |
| | Tucson | 50 | | | | | |
| 10 | Portland | 100 | | B | | | |
| | Douglas County (Oregon) | 45 | | | | | |
| | N.W. Oregon HA | 50 | | | | | |
| | Idaho HA | 150 | | B | | | |
| | Grays Harbor County (Wash.) | 40 | | | | | |
| | Skagit County (Wash.) | 30 | | | | | |
| | Pierce County (Wash.) | 26 | | | | | |

(1) Represents 10 PHAs funded in FY 1988 - 1,459 units.

For FY 1989 46 PHAs were funded - 4,769 units.

SURVEY INDICATORS

- A. Headquarters Officials or staff asked Regional Offices to request funding for specific PHAs from the Headquarters Reserve - 17 PHAs.
- B. PHAs sent requests for funding to Headquarters - 30 PHAs.
- C. PHAs were contacted by former HUD Officials who expressed an interest in obtaining funding allocations - 7 PHAs.
- D. PHAs were contacted by developers who expressed interest in using the Project Based Assistance program - 11 PHAs.
- E. Correspondence from PHAs indicated that fund allocation requests were for specific projects - 10 PHAs.

Appendix B

DISTRIBUTION

Assistant Secretary for Housing - Federal Housing Commissioner, H
 (Room 9100)
 General Counsel, G (Room 10214)
 Deputy Under Secretary for Field Coordination, SC (Room 10126)
 Deputy Assistant Secretary for Multifamily Housing Programs, HM
 (Room 6106)
 Audit Liaison Office, HPAS (Room 9128) (2)
 Director, Office of Budget, AB (Room 10172)
 Director, Office of Elderly and Assisted Housing, EMA (Room 6130)
 Director, Office of Insured Multifamily Housing Development, HMI
 (Room 6134)
 Acquisitions Librarian, Library, AS (Room 8141)
 Director, Financial Management Systems Staff, AFS (Room 5132)
 Regional Administrators - Regional Housing Commissioners (2)
 Directors, Regional Offices of Housing
 Senior Group Director, U.S. General Accounting Office, GAO
 (Room 5250, HUD Building) (2)

Reform of HUD

Under President George Bush
and Secretary Jack Kemp

Clearing the Decks

Ethics

- Sunshine all funding decisions
- Eliminate discretionary funding
- Require registration of consultants and disclosure of fees
- Mandate documented accountability for regulatory waivers
- Increase powers of the Inspector General

Management and Finance

- Appoint a Chief Financial Officer
- Provide resources to ensure adequate program evaluation and monitoring
- Target Block Grants to the needy
- Streamline and strengthen regulatory and audit functions
- Recover misused taxpayer funds

Federal Housing Administration

- Complete comprehensive actuarial study
- Appoint an FHA Comptroller
- Require annual audits and reports
- Eliminate:
 - Title X Land Development Program
 - Vacation home loans
 - Dealer origination of home improvement loans
 - Private investor loans
- Restructure Coinsurance program
- Stop windfall profits from "double dipping" of subsidies



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Part I. ETHICS

ETH-1. Allocation of Housing Assistance -- Sunshine.

- allocate housing assistance using a needs-based formula or a competitive process

Background. This proposal is designed to eliminate the "total discretion" and the "political" emphasis that characterized all too many of the Department's housing assistance programs in the past. Problems were first identified in the Section 8 Moderate Rehabilitation program and in funding from the "Headquarters Reserve." A competitive process with publicly articulated selection factors will help ensure a fair funding system.

Specific Example. Funding for the Section 8 Moderate Rehabilitation program was allocated for years without being subject to any objective criteria. The HUD Inspector General has documented in a 600-page report that the lack of criteria led to a process that was not accountable or controllable.

Reform. This proposal will establish a specific requirement that all incremental housing assistance appropriated to assist families be made either (a) through a formula reflecting the relative need of the area (often referred to as the "fair share" formula), or (b) through a competitive process on predictable cycles. The competitive process will be published in a Notice of Funding Availability (NOFA) with explicit selection criteria, including such factors as the quality of the project and the need for the project in that location. In some cases, such as the Section 202 program for projects for the elderly and handicapped, the assistance will be allocated to urbanized areas and then allocated to particular projects based on a competitive process. Whenever possible formulized allocations to urbanized areas will be used.

Assistance appropriated for special needs will also be awarded based on a competitive process, using explicit criteria, including such factors as the need to correct health and safety conditions and to preserve low- and moderate-income housing. For example, HUD will competitively allocate section 8 rental assistance to projects with FHA insurance where rental assistance is needed, and Flexible Subsidy assistance to FHA projects in need of capital improvements.

Action. Legislative Proposal

ETH-2. Public Disclosure of Allocations and Funding Decisions.

- publish allocations of housing assistance quarterly
- publicly announce all funding decisions

Background. These disclosure requirements respond to criticisms that the Department uses a secret process based on political favoritism to pass out housing assistance.

Specific Example. In the past, the Moderate Rehabilitation program funding was often decided on the basis of political favoritism. This approach would have been discouraged had public disclosure of allocations and funding decisions occurred.

Reform. Quarterly in the Federal Register, HUD will publish its allocations of housing assistance made under section 213(d) of the Housing and Community Development Act of 1974. This will include the Regional Administrator's funding decisions, in cases where allocations are made only to the Regional office level because of the limited amount of funding involved.

In addition, HUD will announce publicly all funding decisions for programs where projects are selected competitively.

Action. Legislative Proposal

ETH-3. Abolish Discretionary Headquarters Reserve Funding.

- abolish discretionary assisted housing headquarters reserve

Background. HUD is currently authorized to reserve up to 15% of the amounts available for housing assistance in a Headquarters Reserve. Amounts in the reserve have been used to fund projects directly from the Central Office without subjecting them to the fair share (pro-rata) formula or to competition.

Specific Example. This proposal will eliminate situations where developers and consultants have persuaded Washington officials to intervene in local funding allocations. Such activities were common under the Moderate Rehabilitation programs.

Reform. The Department will propose a line item in the Department's appropriations act to enable it to hold a limited amount of assistance in Headquarters to fund only:

(i) unforeseen housing shortages due to natural or other disasters, (ii) desegregation efforts, (iii) litigation and (iv) other emergencies.

Action. Legislative Proposal

ETH-4. Eliminate the CDBG Discretionary Fund.

- eliminate technical assistance and special projects funding in the Community Planning and Development discretionary fund.
- allow programs to fund their own Technical Assistance (TA) efforts through a set-aside of program funds.

Background. HUD makes grants to a wide variety of organizations through the Secretary's discretionary fund for technical assistance and other special projects. Many of these have been Congressionally mandated, and have not necessarily been reflective of HUD's own priorities. When used by other program offices within HUD the CDBG connection is sometimes tenuous.

Specific Example. In the case of one TA grant, the recipient spent more than half of the grant on a cross-country quest for municipalities actually in need of the technical assistance. Other examples of waste have been noted; because such funds have been available, Congress has required HUD to fund special projects.

Reform. This proposal would end the use of a separate pool of money for dubious or arbitrary purposes yet assure that legitimate requests for unique types of programmatic assistance may still be satisfied.

Action. Legislative Proposal

ETH-5. Sunshine Waiver of Regulations and Handbooks.

- require that all waivers of regulations granted by the Department be published quarterly in the Federal Register; and
- require that (a) requests for waivers of any HUD regulations be in writing; (b) the decision be in writing and justified on the basis that they are in the public interest or necessary to prevent undue hardship and then only where they are consistent with programmatic or Secretarial objectives; (c) the Assistant Secretary personally grant all waivers of regulations; and (d) that

waivers of handbook procedures (as opposed to regulations) be recorded, justified, indexed and made available for public inspection.

Background. Regulatory waivers can be useful in high cost areas, where mortgage limits and HUD cost containment measure may be too strict to allow projects to be built. HUD officials can permit exceptions to allow low and moderate income projects to proceed. Problems occur, however, when such authority is abused to assist luxury projects whose excessive costs endanger the project and FHA.

Specific Example. In one case in Chicago, HUD officials allowed a developer to undertake various actions which led to FHA financing a high-rise luxury apartment building in which some units rented for \$2,900 per month. Some 1-room "efficiency" apartments were over 1,600 square feet. The project failed economically and FHA paid a \$50 million claim.

Reform. The requirement for publication of waivers of regulations is another sunshine proposal that will assure that only waivers that can withstand public scrutiny are approved. Waivers of handbook procedures will be recorded and maintained.

Action. Legislative Proposal

ETH-6. Inspector General.

- authorize the IG to compel witnesses to testify
- increase IG staffing

Background. The IG's current authority is limited to the subpoena of documentary evidence. The IG can only request witnesses to testify.

Specific Example. It is difficult for the IG aggressively to pursue investigations into fraud, waste, and abuse of HUD's programs without being able to compel testimony from participants and HUD staff. The lack of this authority hindered the IG's ability to pursue investigations into the Moderate Rehabilitation program abuses and other matters in the past.

Reform. This proposal would authorize the IG to issue subpoenas to compel witnesses to testify in connection with IG audits and investigations, and give the IG the same tools Congress has to carry out thorough investigations. As with

other subpoenas, the IG could go to court to enforce refusals

to comply with this subpoena authority. The authority would not, of course, abrogate witnesses' constitutional right against self-incrimination.

Additional staffing will enable the IG to carry out additional audits and investigations of the Department's programs.

Action. Legislative Proposal

ETH-7. Civil Money Penalties.

- authorize the Secretary to impose civil money penalties on:
 - (i) HUD-approved lenders in the FHA full insurance and coinsurance programs;
 - (ii) mortgagors under the FHA multifamily programs;
 - (iii) entities subject to the Interstate Land Sales Full Disclosure Act for violation of program requirements;
 - (iv) approved lenders under GNMA's mortgage-backed securities program.

Background. HUD lacks sufficient tools to assure that participants in its programs comply with program requirements. The applicable criminal penalties are often insufficient to ensure enforcement since problems of proof and limited resources in the offices of the U.S. Attorneys make criminal prosecution difficult.

Specific Example. It is a disgrace that assisted and insured housing projects can be willfully neglected and allowed to deteriorate. Tyler House in Washington, D.C. is an example of a housing development left to decay because of deferred maintenance and repeated violations of housing quality standards.

HUD's hands have been tied in trying to attack these problems early. Its enforcement tools are currently limited to either letters of admonishment or the drastic step of debarment - but nothing in between. Consequently, physical problems mount over many years, ending only when bankruptcy is the last alternative for the owner, and HUD takes possession.

If HUD could have entered the Tyler House situation early and imposed fines for violations of housing quality standards, the situation would not have deteriorated over the years to

such a deplorable state. Instead, HUD could have economically forced the owners and managers to take one of two actions: either make the necessary repairs, or default. A default in such a case would allow HUD to find a responsible owner for the project and save the insurance funds money because the project would not yet have deteriorated to the point of being worthless.

Reform. Authorizing the Secretary to impose civil money penalties for violations of specific program requirements will permit HUD more effectively to deter fraud and other violations by mortgagees and lenders, multifamily mortgagors, developers subject to the Interstate Land Sales Full Disclosure Act, and approved lenders under GNMA's mortgage-backed securities program. The possibility of civil money penalties should also help expedite execution of settlement agreements.

Action. Legislative Proposal

ETH-8. Registration of Consultants.

- require registration by consultants and lawyers
- require disclosure by project sponsors of fees paid
- impose fines of up to \$10,000 for each act of noncompliance

Background. Would-be influence peddlers will be subject to full public scrutiny. This proposal, together with ETH-9, which would authorize a fine for HUD employees who disclose advance information about pending funding decisions, is intended to curtail abuses by consultants and lobbyists.

Specific Example. In the Moderate Rehabilitation program, non-technical consultants were paid up to \$1,000 per unit to arrange funding awards in advance of public notice.

Reform. This proposal would require that consultants and lobbyists doing business on behalf of clients for HUD-funded projects and activities register with the Department. Their clients would be required to disclose the amounts paid to the consultants. Civil money penalties of up to \$10,000 per violation would be authorized in the case of noncompliance. Fees paid to consultants, lobbyists and lawyers will be considered in determining the amount of assistance to be provided.

Action. Legislative Proposal

ETH-9. Prohibition of Advance Disclosure of Funding Decisions.

- \$10,000 fine for HUD employees who release information on pending funding decisions

Background. To promote the integrity of HUD's decision-making process in programs subject to a competitive process, HUD employees must be forbidden from advance disclosure of nonpublic financial information to any individual or entity that could financially benefit from receiving such information.

Specific Example. The Inspector General's audit of the Moderate Rehabilitation program revealed that, in at instance, private consultants presented copies of HUD funding documents to officials of a Public Housing Authority (PHA) -- normally transmitted directly by HUD to the PHA -- and indicated that the funds were theirs (the consultants) to distribute. These documents should not have been in the hands of these outside third parties. At the very least, access to these funding notifications provided those developers with an unfair advantage and may have influenced the PHA's ultimate selections. And in fact, the PHA simply selected these developers and ignored the required competitive procurement.

Reform. This proposal will prohibit advance disclosure of pending HUD decisions that could have the effect of giving unfair financial advantage to any party. HUD staff, including political appointees, responsible for releasing such information would be subject to a civil money penalty of up to \$10,000. Advance notice to Congress would continue.

Action. Legislative Proposal

ETH-10. HUD-Funded Travel Subject to GSA Regulations.

- require HUD-funded travel by HUD-funded grantees to conform to Federal travel standards

Background. Public housing agency employees and employees of other HUD-funded entities occasionally attend meetings and conferences held in vacation spots in hotels that charge more for rooms than Federal guidelines permit for Federal employees. Federal money should not be used to fund travel that does not meet the strict GSA travel regulations which assure strict accountability and modest accommodations.

Specific Example. A recent advertisement for a conference for PHA commissioners that will be held in a luxury coastal

resort illustrates this problem. The ad notes that the resort "is situated directly on the Gulf of Mexico and features wide beaches and sporting activities. Come, learn and enjoy."

Reform. This proposal will require, and enforce, a provision that all HUD-funded travel by any HUD-funded grantee be in accordance with GSA travel regulations.

Action. Administrative

**PART II. HUD MANAGEMENT REFORM, INCLUDING
FINANCIAL MANAGEMENT REFORM**

MR-1. Management Review

- Complete independent comprehensive management review of HUD
- HUD has hired Price Waterhouse to recommend financial and management controls

Background. HUD has suffered from years of poor communications among offices and divisions within HUD, lack of common oversight and control, and a lack of managerial accountability. There is reason to believe that HUD's management structure may contribute to these difficulties. While wholesale reorganization is not likely to be necessary, there are functional problems which need to be studied by outside experts, particularly in technical areas, such as accounting and information systems.

Specific Example. An example of a potential structural problem, is HUD's relative neglect of its multifamily housing management efforts in favor of development. (Management staff monitor owners and managers, look after FHA's real estate and handle property sales. Development staff work on new projects). This may be short-sighted, because heavy losses can be avoided by making sure that projects are run well and maintained. And some of the need for expensive new construction can be met by minimizing vacant and deteriorated units. Management personnel require highly technical financial skills, yet are automatically graded one classification below development staff. At one point, HUD economized on management staff by dropping the policy of making annual on-site inspections of every project.

In 1988, FHA recorded a loss of over \$1 billion on multifamily insurance; a management study can help identify how some of HUD's priorities can be redirected towards saving taxpayer's dollars, and at the same time emphasizing a commitment to well-run projects.

Reform. HUD has initiated a comprehensive management review to identify all structural and systemic changes needed for further reform. In addition, Price Waterhouse will specifically examine and recommend improvements in the financial policies, practices, and controls in HUD's Office of Finance and Accounting.

Action. Administrative

MR-2. HUD Chief Financial Officer

- Appoint a Chief Financial Officer for HUD reporting directly to the Secretary
- Appoint a Comptroller for FHA

Background. In recent testimony on FHA performance, a representative of the Government Accounting Office stated, "an important part of the solution to HUD/FHA's problems is to establish a Chief Financial Officer within HUD and a corresponding comptroller within FHA. A chief financial officer would be responsible for setting accounting and financial reporting policies, directing the development and operation of financial management systems, and ensuring the maintenance of a sound internal control structure. The FHA Comptroller would share the same responsibilities as the HUD Chief Financial Officer, but within FHA."

Specific Example. CFO's are responsible for making sure that cash management systems are tightly controlled. As in the Closing Agent embezzlement episodes ("Robin HUD", etc.), there has been inadequate attention paid to reconciliation of accounts, management reports, and cash tracking. Basically, no one person at HUD (below the Secretarial level) was accountable for making sure that the different program offices and computer systems were working together to prevent fraud.

Reform. Secretary Kemp will appoint a Chief Financial Officer for HUD with broad powers to develop, maintain and oversee the department's accounting, financial control, and cash management systems. In addition, a Comptroller will be appointed for FHA who will oversee the financial operations of FHA. The FHA Comptroller will be accountable to the HUD Chief Financial Officer on general ledger and cash control matters. The FHA Comptroller will report to the FHA Commissioner. Congress will be asked to pass legislation institutionalizing these offices.

Action. Legislative and Administrative

MR-3. Program Financial Management

- A task force has been created to tighten financial management activities
- Complete priority action plans by the end of November

Background. The Secretary created a task force on July 14 to identify systemic management problems in 26 major program and financial management activities of HUD. The task force

will also document their findings and recommend solutions to each problem, and develop an action plan describing implementation of the solutions. Fourteen of these activities were given the highest priority for immediate action. These fourteen cover the majority of HUD's collection and disbursement activities. Action plans for these fourteen will be developed by the end of November and implemented immediately. Action plans for the remaining twelve will be developed and implemented shortly thereafter.

Specific Example. The activities of FHA closing agents are not adequately controlled, allowing closing agents an opportunity to defraud the federal government. The Robin-HUD case is a well-publicized example of inadequate internal controls.

Reform. The Task Force has convened over 70 working group meetings to review documented problems from GAO, IG, OMB, and productivity studies. Action plans identifying major problems and the steps needed to correct them will result from task force analysis.

Action. Administrative

MR-4. Program Evaluation

-- Establish a fund for evaluation and monitoring.

Background. HUD spends \$17-18 billion per year in grants and assistance, but less than \$25 million for evaluation and monitoring. Such expenditures would pay for themselves by averting unnecessary payments and fraud.

Specific Example. The Section 8 program disburses more than \$10 billion annually on behalf of more than 2.4 million households, but does not have complete records regarding the program. HUD is not able to verify the accuracy of subsidy payments. In such a situation, overpayments could be substantial.

Reform. Under this proposal, an amount up to 0.5% of total expenditures would be dedicated to program evaluation and monitoring. The expectation is that these payments will more than pay for themselves in improved service and lower waste.

Action. Legislative Proposal

MR-5. Expedite HUD Rulemaking.

- Streamline legislative review procedure applicable to production of HUD regulations

Background. Legislative review began in 1978 with the adoption of a cumbersome and time-consuming procedure calling for making the effectiveness of HUD rules subject to review by the Banking Committees. While the Committees employ the review as a tool for oversight, existing procedures subject HUD rules to extreme delays and hamper the Department's ability to institute necessary policy and statutory mandates.

Specific Example. Rules to implement the Deficit Reduction Act were published on October 31, 1986 but could not be announced for effect until March 2, 1987 - a delay of approximately four months.

A rule implementing the Freedom of Information Reform Act of 1988 was published by HUD on September 27, 1988 (53 FR 37546), but could not be announced for effectiveness until March 3, 1989 because of the congressional schedule--a wait of 155 days--instead of the 30 days normally required by the Administrative Procedure Act.

In neither of these instances was there ever a suggestion of Banking Committee opposition, in either the House or the Senate, to the substance of the published rules.

Reform. This proposal would amend section 7(o) of the HUD Act to permit more expeditious legislative review of all HUD regulations.

Action. Legislative Proposal

MR-6. Ratify HUD's Section 8 Rent Adjustment Procedures.

- ratify HUD's established Section 8 rent adjustment procedures

Background. HUD's Section 8 rent adjustment procedures are limited by comparability studies, so as to prevent material differences between the rents charged for assisted and comparable unassisted units of similar quality and age in the same market area.

Specific Example. In the Rainier View decision, the 9th Circuit held that HUD had misapplied the statute. One

consequence of this decision was that a for-profit landlord received a check for \$3 million in windfall subsidies and funds that should be used to assist additional families. Often, developers have already been paid up to 120% of market rates.

Reform. If applied nationwide, the Rainier View decision would cost up to \$1 billion in Section 8 subsidies. Ratify the Department's policy of using market comparability to determine Section 8 project rent increases.

Action. Legislative Proposal

MR-7. Improve Block Grant Program Sanctions and Recover Misspent Tax Dollars

- Eliminate cumbersome procedural requirements which impede HUD's ability to recover improperly used CDBG funds.
- retain authority to condition grants on ongoing performance, to litigate compliance problems, and to seek judicial relief
- statutorily expand rights of grantees to consult with HUD prior to imposition of sanctions
- facilitate HUD's efficient management of ongoing performance problems

Background. Because of a recent court decision, HUD may no longer condition or reduce a future grant to compensate for disallowed costs resulting from audits or monitoring. The two courses available now are to provide for a hearing before an administrative law judge, or to bring the matter before the courts. In most cases, the grant funds will have been spent fully, and only the courts can recover already spent funds from a grantee. Thus, hearings before an administrative law judge, in practice, are of limited usefulness to HUD.

Specific Example. HUD has found numerous activities in each of the past several years where counties have spent CDBG funds the county cannot validate. By the time HUD exhausts its current administrative remedies trying to verify the abuse, it is quite likely that all the funds will have been spent by the county.

Reform. For cases of continuing performance problems, this legislation authorizes HUD to apply sanctions to past and future grants, in ways that guarantee the rights of grantees. The opportunity to seek judicial relief in cases of past substantial noncompliance is preserved. The proposal would

assure that HUD has more effective legal remedies at hand than now exist to assure proper use of its funds.

Action. Legislative Proposal

MR-8. Section 235 Refinancing

-- initiate a program to offer incentives to homeowners to encourage refinancing of FHA-insured home loans.

Background. Many homes purchased under the Section 235 program for low income homeownership carry mortgages at high interest rates. Because HUD pays interest above a certain rate, it will realize all of the savings if the owner refinances to a lower rate. Because the owner realizes no savings, he has no incentive to refinance.

Specific Example. At current market rates, the U.S. Treasury could recover an estimated \$200 million by refinancing. In 1986 (before many participants left the program) HUD's Inspector General estimated the figure at almost \$800 million.

Reform. The Department will undertake an initiative to refinance Section 235 mortgages. This will require incentives for owners in the program to refinance.

Action. Legislative Proposal

MR-9. Bankruptcy Code

-- exempt actions taken by HUD from the automatic stay provision of the Bankruptcy Code.

Background. Under current law, we may commence, but not proceed with foreclosure after a bankruptcy petition has been filed. This proposal would exempt from the automatic stay provision of the Bankruptcy Code actions taken by HUD to carry out and complete foreclosure of multifamily projects.

Specific Example. The HUD office in Boston had one project that defaulted in 1977, but could not be foreclosed until 1989.

Reform. This would permit HUD to protect the interest of the Department and the tenants in the project.

Action. Legislative Proposal

MR-10. Target CDBG Better To Low and Moderate Income Persons

- tighten the accounting rules to end distortion of reported benefits by requiring proportionate accounting
- increase to 75% the overall low/mod benefit requirement
- provide for more effective targeting of funds in more affluent communities by requiring 100% of activities to address the low/mod benefit objective

Background. Under existing law, CDBG grantees can spend up to 40% of their funds for activities which do not benefit low and moderate income persons. Moreover, activities

assisted with the balance of funds may benefit a substantial proportion of people who are not low or moderate income. As a result, the actual proportion of funds spent by some communities to benefit low and moderate income persons can be substantially less than 50%.

Specific Example. One wealthy suburban community used CDBG funds to plant trees, and install bike racks and benches. The funds could have gone instead to other parts of the county which have profound housing and economic development needs. The new proposals would make it highly unlikely that the county could fund these sorts of activities.

Reform. These proposals, taken together, would assure that scarce resources are targeted more effectively and that both HUD and Congress are more realistically informed as to who actually benefits from CDBG expenditures.

Action. Legislative Proposal

MR-11. CDBG Antipoverty Strategy

- require entitlement grantees and states to have a strategy for fighting poverty

Background. The CDBG allocation formulas provide funds to recipients, in large measure, because of the extent of poverty within their jurisdictions. There is, however, no program requirement that funds be used by the recipients to reduce actively the incidence of poverty.

Specific Example. A large city in the Sunbelt, over several years, has spent the bulk of its CDBG funds on the

redevelopment of its downtown district -- not on fighting poverty.

Reform. This proposal would bring recipients of CDBG funds into partnership with HUD as it wages a new war on poverty and require them to think through a CDBG strategy consistent with federal goals.

MR-12. Redemption of Foreclosed Properties

Background. In many states, the Department incurred a loss on foreclosed property it could not sell because FHA was required to abide by State mandated redemption periods. When legislative relief was granted to FHA programs, the same protections were not afforded properties under the Section 312 program.

Specific Example. In the case of a property which stands vacant for a year due to redemption rights, the Department can lose its entire loan investment due to vandals or deterioration.

Reform. The Department seeks the same preredemption rules for the Section 312 community development loans as it has for FHA single family program.

Action. Legislative Proposal.

MR-13. Moderate Rehabilitation Reform

Background. Internal investigations have uncovered patterns of favoritism and abuse in the selection of projects for funding under the Moderate Rehabilitation Program.

Specific Example. In one case, local officials had not requested assistance for an area, yet units were provided, throwing into question the priorities and methods used to make funding decisions.

Reform. Funding for the Section 8 Moderate Rehabilitation Program has been proposed for termination by Congress; the Department will use programs such as the project-based certificate program, the low income housing tax credit, community development block grant, the rental rehabilitation program, and public housing modernization funds to help accomplish our goals for rehabilitating public and assisted housing. HUD is proceeding with nationwide audits of 277 Moderate Rehabilitation projects funded from 1984 to 1988. If excessive subsidies are being paid, HUD will pursue measures to recapture those funds.

PART III. FEDERAL HOUSING ADMINISTRATION

I. MANAGEMENT AND ACCOUNTABILITYFHA-1. Require Annual Audited Financial Statements for FHA

Background. Annual audited financial statements are the most basic of all management requirements. In a financial operation, the top-level reports drive all lower-level systems, and systems deteriorate without the discipline of rigorous annual review at the top. In particular, insurance operations require both cash-based and accrual-based records.

Yet FHA did not have annual audited reports from 1974 until 1989, and its internal reports only measured results on a "cash basis." The result was an absence of necessary accounting controls and reporting.

Specific Example. From 1974 to 1989, FHA's finances were not audited by an outside accounting firm. For fifteen years, therefore, public accountability was limited. The General Accounting Office (GAO) attempted audits in 1981 and 1984, but FHA's books were in such disarray that the preparation of financial statements was impossible. In 1987, GAO began again, this time spending two years working with Price Waterhouse and HUD's accounting department to develop systems capable of measuring the agency's finances.

FHA did, however, produce internal financial statements. But these were done for the most part on a cash basis, not the accrual basis necessary to accurately portray an insurance operation's condition. FHA's managers therefore had an unrealistically rosy picture, because claims were only counted when they were paid, not when the default occurred.

On September 27, 1989, the U.S. Comptroller General (the GAO administrator) reported to Congress that full financial statements for FHA had been completed. These statements showed a \$4.2 billion accrual basis loss in FY 1988. FHA had reported a \$856 million loss for the same period on a cash basis.

The difference in the two amounts was that a large number of defaults and delinquencies had occurred in 1988. FHA will have to pay for these over the next two to three years. By analogy, there is a difference between the balance recorded in a checkbook (the accrual basis) and the balance showing on the screen of the automatic teller (the cash basis). In essence, FHA has many outstanding "checks"; these were not recorded and will soon be cashed.

Reform. HUD will require and publish annual audited financial statements, prepared by an independent accounting firm. These statements will be on both a cash and accrual basis, and will be consistent with generally accepted accounting procedures. The auditors will also be asked to provide a Management Letter pointing out deficiencies in FHA's financial control and management systems. Secretary Kemp announced this policy in a letter to Senators Alan Cranston and Alfonse D'Amato on August 3, 1989.

The FHA Comptroller (see MR-2) will be responsible for ensuring that all accounting systems are well-managed and capable of being fully audited every year. Results will be consolidated with the HUD general ledger under the auspices of the HUD Chief Financial Officer and will be transmitted to Congress and published each year.

Action. Legislative Proposal

FHA-2. Commission Independent Actuarial Analysis

Background. FHA operates 47 different insurance programs. Because economic and technological changes have affected the viability of many of them, a reassessment of FHA's basic financial exposure is necessary.

Specific Example. Although it has over \$300 billion of insurance-in-force, FHA has only one certified actuary. By contrast, the Prudential Insurance Company has 150 actuaries.

Reform. An independent actuarial study has been commissioned by HUD. This effort will include the development of a computer model that FHA managers can use to test the impact of rapidly changing economic conditions, the effects of proposed legislative initiatives, and the effect of various terms and conditions on the viability of policies.

FHA will also hire additional actuaries and develop an ongoing review process for all insurance programs.

Action. Administrative

FHA-3. Unify FHA Program and Accounting Functions

Background. FHA's programmatic divisions (underwriting, management and monitoring) report to the FHA

Commissioner, while the accounting divisions report through another line of authority to the Assistant Secretary for Administration. This split of FHA was ordered in the early 1970s - the same time that audited financial statement became difficult to produce. Two problems have resulted: (i) program managers are not accountable for finances, and (ii) accounting and processing are not accountable to program needs.

Specific Example. When the new FHA appointees interviewed one program manager about the losses in his program, he had no idea how large they were - the accounting people would know. The accounting people didn't know. They'd never been asked. It took Assistant Secretary-level orders from both FHA and Administration to produce a rudimentary loss estimate (about \$170 million).

Similar incidents have occurred during the reviews of nearly every program. The avoidance of financial accountability in FHA has become cultural and pervasive.

Reform. A Comptroller will be appointed within FHA to oversee cash flows and to direct business operations. The FHA Comptroller and FHA accounting and insurance processing functions will report to the FHA Commissioner. The Commissioner will therefore be accountable for the financial operations of FHA, and will ensure that both program and accounting managers are required to work together. All FHA accounting will be consolidated into the HUD general ledger under the Chief Financial Officer.

Action. Administrative

FHA-4. Require Program-by-Program Accounting

Background. Currently, no accounting records break down financial results by program. Instead, all profits and losses are lumped together into arbitrary totals. Without accounting by "section of the Act," Congress cannot judge the efficiency of housing programs it creates, and managers inside FHA have no feedback on the operations of their own programs. Such accounting systems formerly existed, but were dropped ten years ago.

As GAO noted in testimony before the Senate Banking Committee,

"At present, managers at FHA do not have sufficient program-level financial information to determine which programs are self-sustaining and which are not... Financial information is periodically produced only for each of its four major funds."

Specific Example. Title I Manufactured Housing mortgage insurance has apparently sustained hundreds of millions of dollars in losses in recent years. We say, "apparently," because no one can tell for sure; HUD's computer systems cannot distinguish between Manufactured Housing's losses and those of coinsurance, hospitals, Title I, and other programs consolidated in the General Insurance Fund.

Reform. HUD will institute "section-of-the-Act" accounting by FY 1991.

Action. Administrative

FHA-5. Require Region-by-Region Accounting

Background. HUD operates through ten regional offices around the country. The Regional Administrators are responsible for the management of programs in their areas; they allocate staff, set priorities, etc. Yet they are told nothing of the financial conditions of operations in their regions because HUD produces no surplus/deficit reports broken down by region. The Comptroller General of the GAO cited this deficiency in his September 27 report to the Senate Banking Committee.

This would be analogous to a division president at General Motors not knowing his division's finances, and his superiors not knowing either. Accountability is impossible.

Specific Example. Five of the regional housing directors were recently asked to name the top three causes of FHA losses in their regions. None could; in fairness, such information is a Headquarters responsibility, and Regional Administrators have continually asked for better information.

Reform. HUD will institute Region-by-Region accounting for FY 1991.

Action. Administrative

FHA-6. Institute Processing Improvements

Background. FHA processes over one million applications per year. It services over 6.8 million policies. Yet the capabilities and integration of

FHA's processing and computer systems are not modern. Major upgrades are necessary in all systems, and the distribution of processing functions in the field require rationalization to improve efficiency.

Specific Example. FHA's operations are split among several mainframe computer systems, each in a different location and different languages. It is not surprising that accurate information is so hard to assemble and that processing delays are so common.

GAO has cited, for example, the fact that FHA has two overlapping automated systems for managing its single family housing inventory. This is obviously redundant, and is a further problem because the numbers produced by each have grown alarmingly in disparity.

Thus, in the case of "Robin HUD", FHA had two conflicting systems tracking the closing agent's sales. And neither of these computers was talking to the one recording the cash proceeds of the sales. Dishonest closing agents have exploited the gaps in HUD's financial controls.

Reform. (i) HUD will fully integrate all FHA systems by FY 1992. This will either require a new mainframe to replace the current four, or a major software and communications integration effort. (ii) HUD will institute an Assistant Secretary-level review committee to set computer budget priorities. This committee has already begun work under the direction of the Undersecretary. (iii) HUD will review field processing operations for potential economies of scale in consolidation of processing functions.

Action. Administrative

2. SINGLE-FAMILY HOUSING: Back-to-Basics

FHA-7. Prohibit Private Investors

Background. FHA's single-family insurance programs are designed to provide homeownership opportunities for families who will occupy their own homes. FHA does not exist to provide profit opportunities to private investors. Investors are much more likely to walk away from their homes in an economic downturn and are responsible for the majority of the fraudulent schemes in FHA programs.

Specific Example. Investors are only a small portion of FHA's business, but a significant source of its troubles. In 1988, investors accounted for only 2.5% of FHA's new policies, and roughly 15% of the losses. Most of the defaulting loans were written in earlier years. One group of private investors in Denver owned 750 FHA homes, and defaulted on every one of them.

Reform. In the future, private investors will be excluded from FHA insurance of single family homes they do not occupy. Still accepted would be public purpose investors, such as state and local housing finance agencies and non-profit housing providers. Multi-unit owner-occupied structures also will be permitted, as for example a family occupying one unit of a duplex while renting out the other.

By this reform, HUD is not seeking to discourage private investment in housing as a general matter. The reform is rather a recognition that the federal government should not subsidize the risks of private speculation, and that private sector investment will be more wisely allocated at free market rates.

Action. Legislative Proposal

FHA-8. Prohibit Dealers and Loan Brokers from Originating Title I Home Improvement Loans

Background. Currently, home improvement contractors (for example, exterior siding salesmen) help their customers complete and submit Title I loan applications for the work they do. Similarly, loan brokers earn fees by obtaining Title I loans for borrowers. The inherent conflicts of interest in these arrangements are obvious. The unscrupulous contractor can advance his interests at FHA's expense.

Specific Example. Home improvement contractors have been

known to "help borrowers qualify" by inflating their incomes or hiding debts. Contractors often do shoddy work or overcharge. Loan brokers have assisted borrowers in

obtaining Title I loans for ineligible items (e.g., personal loans, swimming pools, debt consolidation). One loan arranged through a loan broker was used to finance the borrower's divorce--even though the application stated that it was for home improvements.

Reform. Dealers and loan brokers will be prohibited from assisting in the preparation or submission of Title I Home Improvement loans.

Action Required. Legislative

FHA-9. Restructure Title I Manufactured Home Loans Program

Background. In current practice, dealerships for manufactured homes can commit FHA to insuring loans on manufactured homes (mobile homes) that they sell. The lenders in between the dealer and FHA have not questioned most applications. Again, a conflict of interest exists: the salesman has an interest in qualifying the applicant in the face of adverse credit criteria, and has incentive to inflate the mortgage amount. Numerous cases of fraud have been discovered. The manufactured home loan insurance program has cost FHA and GNMA over \$500 million in recent years.

Specific Example. A common scheme was for a dealer to finance the purchase of the furniture as well as the home itself (an accepted practice in the industry) then take back some of the furnishings as the "down payment".

Reform. FHA, GNMA and the manufactured housing industry will meet to revise and restructure the lending process for FHA manufactured housing home insurance.

Action Required. Regulatory

FHA-10. Restrict Second Home Loans

Background. Under existing law, an FHA borrower can qualify as an "owner-occupant" for more than one home. In addition to a "principal residence" that is the borrower's primary home, he can obtain an FHA loan for a "secondary residence" which he occupies for part of the year. HUD has administratively required a 15% downpayment on secondary residences.

Specific Example. The most common form of "secondary residence" is a vacation property owned by a family wealthy enough to afford a beach house or a ski lodge. In effect, these secondary residences are actually high-risk investment properties that double as a weekend retreat for the owner. FHA should not be used to insure these sorts of properties.

In the 1987 Act, Congress had repealed HUD's Section 203(m) authority to insure "vacation homes". Unfortunately, a loophole remained in that vacation homes could often be insured as "second homes".

Reform. HUD will close all vacation home loopholes. In the future, FHA will only insure second homes in bona fide hardship cases (e.g., where a family moved to a new area for purpose of employment and had been unable to sell their existing home -- or where a second home could be justified on the basis of seasonal employment). However, FHA will not insure second homes used for investment or vacation purposes.

Action. Legislative Proposal

FHA-11. Require Credit Checks for Loan Assumptions

Background. FHA loans are currently assumable without restriction: an owner can hand their house keys to anyone they wish and FHA is liable. For investors, current law requires a credit check if the transfer is done in the first two years of a loan. Monitoring has been lax, and abuse has been common. "Straw buyer" fraud, "equity skimming," and unsuitable buyers have been particular problems.

Specific Example. In Houston, two investors advertised in newspapers that they would "assume" FHA loans from borrowers who were unable to continue making payments. The borrowers actually paid these individuals \$1,000-\$3,000 to take title to their property, believing that the sale would protect their credit rating. Instead, the investors rented the properties and never paid the mortgage. In dozens of cases, the investors pocketed the rents, FHA paid the claim and suffered a loss and the original borrowers found themselves disqualified from buying new homes.

Reform. All buyers assuming an FHA loan will be required to be checked for history of FHA-related problems, and a basic credit check. A full underwriting analysis will not be necessary.

Action. Legislative Proposal

FHA-12. Terminate Title X

Background. Of the 58 Title X Land Development Insurance policies that FHA has endorsed since 1977, 25 have defaulted. Losses are estimated to total almost \$100 million. The program was designed to help develop subdivisions, but went to build highly speculative upscale residential communities with little regard for affordable housing.

Specific Example. One defaulted Title X loan was used to build a development on a golf course in Palm Desert, California.

Reform. The Title X Land Development Insurance Program will be terminated through rulemaking at HUD, with a request for legislation to ratify the repeal.

Action. Regulatory

FHA-13. Provide Authority for Regional Underwriting Criteria

Background. America's economy is becoming increasingly regionalized, particularly in its housing markets. Regional economies can be isolated from the rest of the country, as recent experience in the oil-producing states has demonstrated. Yet FHA's underwriting criteria and standards are national. Regional directors do not have the flexibility to respond to special needs in their regions or the control speculative excesses.

In particular, FHA should be able to specifically target inner city areas, underserved rural areas, and populations which can benefit from FHA homeownership programs but may be outside of the mainstream of mortgage finance. In many ways, these groups can be strong credits and provide a healthy diversification for FHA's insurance portfolio.

Specific Example. In Houston, the local office owned over 5,000 repossessed homes, yet continued to fuel the soft market with new insurance for speculative investments in new subdivisions.

At the same time, FHA insured only four high loan-to-value single family loans in all of the Bronx, New York - in large part because underwriting criteria could not be targetted to the special conditions of that area.

Reform. Limited authority will be given to regional offices to adjust underwriting criteria given the needs imposed by local conditions. The limits of such authority will be specified in regulation. The FHA Commissioner will also develop a policy on methods of targetting underserved groups. The FHA Commissioner will establish national criteria for limits to such authority with twin goals of nationwide actuarial soundness for the Mutual Mortgage Insurance Fund and the public purpose of enhancing homeownership opportunities.

Action. Regulatory

FHA-14. Review Incontestability Policy in Cases of Fraud

Background. FHA does not contest claims for payment unless it has grounds to refuse payment because of lender fraud. There are gray areas, however, where the lender was involved in a fraud perpetrated by the mortgagor, or actively knew of it and did nothing. FHA needs to clarify its position on such cases, both to free itself to pursue fraudulent lenders and to reassure the secondary market of its basic incontestability policy.

Specific Example. Mortgage companies have knowingly originated large numbers of fraudulent loans for sale to other mortgage bankers. The purchasing investor then discovers that the FHA mortgage insurance premium hasn't been paid or the loan hasn't been endorsed for FHA insurance. In one fraud case, a lender purchased several hundred mortgages that are not eligible for FHA insurance because the were fraudulently closed. The original lender has since gone out of business.

Reform. A formal policy will be developed by the FHA Commissioner, the GNMA President and the HUD General Counsel regarding claims contestibility in cases of known fraud.

Action. Administrative

FHA-15. Require State or HUD Certification of Appraisers

Background. Currently, there are no training requirements for appraisers in some FHA programs,

although some have experience requirements. FHA's whole appraiser qualification policy lacks consistency and minimum standards. The Financial Institutions Reform, Recovery and Enforcement Act of 1989 requires states to create certification processes for appraisers in their states.

Specific Example. Area Management Brokers are private contractors (in the same manner as closing agents) who are delegated many management responsibilities in the handling of FHA's single family housing inventory. Among these is the task of setting the asking price for FHA's property sales, yet they need no valuation credential and in fact have a financial interest in setting an unreasonable price.

Reform. Appraisers involved in the underwriting of FHA programs will be required to be certified under the new state certification rules subject to applicable Federal acquisition requirements. Area management brokers will be required to be certified appraisers, or undergo standardized FHA valuation training. During the phase-in of these requirements, FHA staff appraisers will conduct reviews of appraisals and valuations submitted.

Action. Regulatory

FHA-16. Control Quality of Program Participants

Background. FHA has in the past ten years delegated a wide variety of its processing activities to thousands of widely scattered firms - mortgage bankers, closing agents, area management brokers, fee appraisers, etc. The quality of FHA's business depends on the quality of this infrastructure. To the extent the strongest institutions avoid FHA (because of slow service, inappropriate products, etc.), FHA will find itself having to spend more time monitoring and controlling a weaker network.

Specific Example. In 1988, only two of the nation's top ten mortgage lenders did significant business with FHA programs.

Reform. Develop and implement a long-term strategic plan to develop the quality of FHA products, improve service to large financial institutions, and undertake marketing efforts designed to strengthen diversity of types of lending institutions, capital requirements, and accountability of insurance distribution networks. HUD will also take steps to improve its contracting and

procurement operations in the field. This will include increased monitoring and increased emphasis on professional contract management in the field.

Action. Administrative

3. MULTI-FAMILY HOUSING: Sound Financial Basis

FHA-17. Coinsurance Reforms

Background. In anticipation of unacceptable losses (\$960 million disclosed in the September 1988 financials with future losses likely), Secretary Kemp in May of this year placed the Coinsurance program under a moratorium to new entrants and initiated a 120-day study period. Problems in the coinsurance industry mirrored those of the S&L industry: irresponsible lending, low capitalization, poor business analysis, and weak enforcement. Improper financial incentives stimulated several large coinsurers to originate large mortgages which were not justified by the underlying value of the mortgaged real estate.

Despite these huge losses, the coinsurance program, properly reformed, can make a substantial contribution toward our affordable housing goal. For example, the average coinsurance mortgages are \$26,000 and \$47,000 under the refinancing and new construction programs, respectively (as compared to an overall \$62,000 single family FHA mortgage). Such mortgages create housing that is affordable by persons with incomes below the U.S. median. Over 332,000 housing units, including 45,000 new or substantially rehabilitated units, have been financed under coinsurance.

Specific Example. DRG Funding Corporation was suspended by Secretary Kemp on March 26, 1989. To date, It has experienced defaults on 113 of its 214 loans, totalling \$709 million out of approximately \$1.1 billion coinsured mortgages which it originated -- a 66% default rate. Charges of improprieties are now being investigated by the FBI.

Reform. HUD is expediting a reform package which will provide for: (i) improved quality standards for coinsurers, including more stringent entry standards, higher capital requirements, and new financial disclosure requirements, (ii) higher cash requirements of developers, (iii) reorganization of the coinsurance division together with acquisition of new skills such as CPAs and appraisers; and (iv) a combination of stricter underwriting standards and monitoring, together with a continuation of the increased enforcement activities initiated by Secretary Kemp who has already sanctioned 10 of the 39 active coinsurers--a record that contrasts with prior lax enforcement.

FHA will pursue the operation of the coinsurance program on a self-supporting basis in order to prevent the use of insurance losses as uncontrolled subsidies.

Action. Regulatory

FHA-18. Revise Property Disposition Requirements for Multi-family Projects

Background. Current law requires HUD to target scarce subsidy resources to previously non-subsidized projects where the mortgage is in default, or the Secretary holds title. HUD must provide 15-year rental subsidy contracts for each unit in a project that on the date of a mortgage assignment are occupied by low- and moderate-income persons. Additionally, if the Secretary of HUD owns the project through a foreclosure action, HUD must provide 15-year rental subsidy contracts for each vacant project unit.

Current law additionally requires HUD to provide 15-year rental subsidy contracts for all units in subsidized or formerly subsidized projects assigned to HUD or owned by the Secretary of HUD. A "subsidized" project is defined as a project where housing assistance payments are made to more than 50% of the units in the project.

In most cases, non-subsidized properties in soft markets enter default status due to high vacancies or a downward trend in rents. Targeting rental subsidies to geographic areas with high unit vacancies, and therefore downward pressure on rents, is inconsistent with a HUD goal to provide project-based subsidies to areas in most need. Areas in most need are generally those with low vacancy rates fostering a shortage of affordable housing opportunities, and upward pressure on rents.

In addition, requiring HUD to place low income restrictions on project units which are not currently occupied by low income tenants may reduce the value of the project to prospective purchasers, and increases potential losses to the FHA insurance fund when the property is sold.

Specific Example: For example, when a HUD property is sold in Houston, where vacancy rates are over 10%, HUD is required to provide 15-year Property Disposition Section 8 funds irrespective of vacancy rates. HUD does not have an opportunity to allocate those same funds to "tight" rental markets where affordable housing is most needed. And HUD may also experience a greater loss to the FHA insurance fund due to the reduced value.

Reform: HUD needs the flexibility of the regulatory process

to describe the type of subsidies most appropriate to care for tenants in projects acquired by the Secretary, or projects in default with the mortgage assigned to the Secretary.

HUD proposes legislation to limit the requirement of maintaining foreclosed properties for low income use to those units which were either (i) subsidized, or (ii) occupied by low income persons at the time of assignment, or the time the Secretary acquired title, whichever is greater. The measure will also give HUD the flexibility to serve low income eligible units with either project-based or tenant-based subsidies.

HUD should evaluate the particular market conditions and specific project conditions to achieve the greatest benefit to the tenants at the least cost to the federal government.

Action: Legislative Proposal

FHA-19. Revise Multi-Family Property Disposition Procedures for Full Insurance Programs

Background. No policy is in place for determining the method of disposition for properties in the subsidized HUD-held or HUD-owned multifamily portfolio. The profit potential for the sponsor, the future fate of the tenants, and the cost to the federal government may be significantly affected by a decision to structure a negotiated sale to a qualified sponsor rather than initiate a competitive bid procedure.

Specific example. Under present policy, negotiations may be initiated by a prospective purchaser of a low-income housing project before HUD has given full consideration of other offers. In the absence of competition, an award granted by HUD to a housing sponsor through a negotiated sale may allow excessive amounts be conceded to the sponsor.

Reform. Develop and implement criteria for decisions leading to the disposition of property in a negotiated sale, and to establish when to initiate a competitive bid procedure. Develop and implement a format to consistently document the application of the criteria.

Action: Regulatory and Administrative

FHA-20. Review Multi-Family Program Terms

Background. Mortgage insurance premiums often do not provide adequate compensation to HUD for the risk associated with insuring multi-family housing. The potential losses incurred are not balanced with the premium received, jeopardizing the stability of the insured portfolio.

Specific Example. Multi-family full insurance programs enlist a "soft-market policy" to insure properties in regions currently experiencing high vacancy rates. The policy allows insurance to be committed for those properties in smaller sub-markets that can be successfully underwritten, but does not allow an increase in the premium charged to cover the additional risk.

Reform. An actuarial study of HUD program performance will be produced to provide a basis for interpreting the additional risk associated with meeting important social objectives. Program and policy changes will be adopted to prospectively equate the risk to the insurance premium and the social benefit.

Action. Administrative

FHA-21. Low Income Housing Tax Credit

Background. The amount of HUD subsidy dollars provided for low-income housing projects is primarily calculated from amounts necessary to service project debt, and pay for project operations. When a project sponsor uses the Low Income Housing Tax Credit (LIHTC) in conjunction with other federal subsidies, the amount of funds available from the sources of funding (rent subsidies and the proceeds from the sale of tax credits) may exceed project development costs to produce windfall profits.

As a result, project sponsors are able to charge high front-end fees for rehabilitating currently subsidized properties, or developing additional subsidized properties. Also, sponsors purchasing properties can pay excessive purchase prices to previous owners due to additional proceeds derived from the combination of funding sources.

Until recently, HUD did not fully analyze the LIHTC when assessing the necessary level of federal government contribution necessary to produce, rehabilitate, or transfer multi-family housing projects. In the past, HUD has reviewed the sources and uses of funds associated with the tax credit, but had no policy to apply the information to the funding of a project.

In many instances state governments, assigned the duty of allocating the LIHTC, have not adequately assessed the level of federal subsidies being provided by HUD, and consequently have not adjusted the level of the tax credit.

HUD is currently in the best position to adjust the subsidies available to the project following disclosure of the amount of funds being raised from the LIHTC.

Specific Example. A low-income housing project was recently sold to a purchaser who secured low income housing tax credits. The LIHTC was used in combination with HUD rental subsidies.

The total cost to rehabilitate the project was estimated to be over \$16 million. The cost of the repairs will be supported by an increase in project rent subsidies.

The \$16 million rehabilitation cost allowed the sponsor to raise a total of \$7.6 million in LIHTC proceeds. Of the \$7.6 million, only \$1.8 million went to pay for the project repairs. The rest of the funds went to pay the sellers of the "failed" project nearly \$4 million, with another \$1.4 million of remaining funds in reserve accounts that may eventually revert to the current owner. The remaining \$400,000 went to pay transaction costs. It is also important to note that the sponsor in control of the sale remained the same, substituting one limited partnership entity with another.

Reform. In order to require project sponsors and real estate syndicators to maximize the amount of tax credit syndication proceeds available to pay for the construction and rehabilitation of low income housing, HUD will analyze the value of the LIHTC and adjust accordingly the amount of federal subsidies available to the project.

Action. Administrative Order



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
THE SECRETARY
WASHINGTON, D.C. 20410-0001

October 31, 1989

Honorable Thomas S. Foley
Speaker of the House
of Representatives
Washington, D.C. 20515

Subject: Proposed "Department of Housing and Urban Development
Reform Act of 1989," and a bill to amend the Bankruptcy
Code

Dear Mr. Speaker:

I am pleased to present to the House of Representatives two bills designed to help eliminate the systemic flaws in existing housing and community development programs, which have made them susceptible to waste, fraud, abuse and political influence, and to restore ethical integrity to the administration of the programs of the Department of Housing and Urban Development. These legislative initiatives are urgently needed to help reform the Department and permit the Bush Administration to pursue its agenda for creating opportunities for homeownership, jobs, and hope in our nation's inner cities and distressed rural communities.

These proposals reflect the many good ideas and recommendations of my staff, of HUD's Inspector General, the General Accounting Office, as well as those offered and introduced by Members of Congress. I am also pleased by the recognition in Congress that this reform is an urgent priority, which requires nothing less than complete bi-partisan support.

Mr. Speaker, among the several provisions contained in the legislative package are:

- A proposal to institute fair and open competition for federal housing funds.
- Proposals to eliminate discretionary funding and require public notification of all funding decisions and housing assistance allocations.
- A proposal to require all consultants doing business with HUD to register with the Department and to fully disclose their fees. This proposal will complement action already

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taken by Congress, as contained in the Department of the Interior Appropriations Act of 1989 (P.L. 101-121).

- A requirement that all regulatory waivers be published in the Federal Register.
- A proposal to earmark for all HUD programs funding to support adequate evaluation and monitoring.
- A proposal to ratify the Department's policy of using market comparability in granting rent increases for low-income housing projects and prohibit the Department from making windfall payments of more than \$2 billion to private owners.
- Proposals to better direct scarce Community Development Block Grant (CDBG) funds to activities which serve low- and moderate-income individuals and to require the establishment of an anti-poverty strategy by all CDBG grantees.
- A proposal to establish at HUD a Chief Financial Officer to supervise the financial management of the Department's programs.
- A proposal to streamline the process for Congressional review of HUD regulations.
- Proposals to restore financial soundness to FHA mortgage insurance programs, including the termination of high-risk programs for land development and vacation homes.
- A bill to amend the Bankruptcy Code governing the powers of a bankruptcy court and the effect of automatic stays on multifamily housing to protect the financial interests of the Federal government.

Section-by-section explanations and justifications accompany this letter and more fully set forth the contents of the bills. I request that the bills be referred to the appropriate committees and urge their immediate enactment.

The Office of Management and Budget has advised that there is no objection to the submission of these draft bills to the Congress and that their enactment would be in accord with the program of the President.

Very sincerely yours,


Jack Kemp

OCT 30 1989

A BILL

To amend Federal laws to reform housing, community and neighborhood development, and related programs, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Department of Housing and Urban Development Reform Act of 1989".

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TITLE I -- ETHICS

ALLOCATION OF HOUSING ASSISTANCE

SEC. 101. (a) ASSISTANCE SUBJECT TO FORMULA

ALLOCATION. --(1) Section 213(d)(1) of the Housing and Community Development Act of 1974 is amended to read as follows:

"(d)(1)(A) Except as provided by subparagraph (B) of this paragraph, the Secretary shall allocate assistance referred to in subsection (a)(1) of this section the first time it is available for reservation on the basis of a formula that is contained in a regulation prescribed by the Secretary, and that is based on the relative needs of different States, areas, and communities, as reflected in data as to population, poverty, housing overcrowding, housing vacancies, amount of substandard housing, and other objectively measurable conditions specified in the regulation.

"(B) The formula allocation requirements of subparagraph (A) of this paragraph shall not apply to --

"(i) assistance that is approved in appropriation Acts for use under section 9, 14, or 17 of the United States Housing Act of 1937;

"(ii) other assistance referred to in subsection (a)(1) of this section that is approved or designated in appropriation Acts for uses that the Secretary determines are incapable of geographic allocation on the basis of the formula described in

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subparagraph (A) of this paragraph, including (but not limited to) amendments of assistance contracts; renewal of assistance contracts; assistance to families that would otherwise lose assistance due to the decision of the project owner to prepay the project mortgage or not to renew the assistance contract; assistance to prevent displacement or to provide replacement housing in connection with the demolition or disposition of public and Indian housing; and assistance in support of the property disposition and loan management functions of the Secretary; or

"(iii) other assistance referred to in subsection (a)(1) of this section that is approved or designated in appropriation Acts to be provided to target areas with greater needs, subject to the competition requirements specified in paragraph (5)(B) of this subsection.

"(C) Any allocation of assistance under subparagraph (A) of this paragraph shall, as determined by the Secretary, be made to the smallest practicable area, consistent with the delivery of assistance through a meaningful competitive process designed to serve areas with greater needs.

"(D) Any amounts allocated to a State or areas or communities within a State that are not likely to be used within a fiscal year shall not be reallocated for use in

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another State, unless the Secretary determines that other areas or communities within the same State cannot use the amounts within that same fiscal year."

(b) **ALLOCATION TO NONMETROPOLITAN AREAS.** -- The second sentence of section 213(d)(2) of such Act is amended by striking out "such assistance" and inserting in lieu thereof the following: "the assistance that is subject to allocation under paragraph (1)(A) of this subsection".

(c) **COMPETITION FOR ASSISTANCE.** -- Section 213(d) of such Act is amended by adding the following new paragraph at the end thereof:

"(5)(A) The Secretary shall not reserve or obligate assistance subject to allocation under paragraph (1)(A) of this subsection to specific recipients, unless the assistance is first allocated on the basis of the formula contained in that paragraph and then is reserved and obligated pursuant to a competition.

"(B) Any competition referred to in paragraph (1)(B)(iii) or (5)(A) of this subsection shall be conducted pursuant to specific criteria for the selection of recipients of assistance. The criteria shall be contained in --

"(i) a regulation promulgated by the Secretary after notice and public comment, or

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"(ii) to the extent authorized by law, a notice published in the Federal Register.

"(C) Subject to the times at which appropriations for assistance subject to paragraph (1)(A) of this subsection may become available for reservation in any fiscal year, the Secretary shall take such steps as the Secretary deems appropriate to ensure that, to the maximum extent practicable, the process referred to in subparagraph (A) is carried out with similar frequency and at similar times for each fiscal year.

"(D) This paragraph shall not apply to assistance referred to in paragraph (4).".

(d) **APPLICABILITY.** -- In accordance with section 201(b)(2) of the United States Housing Act of 1937, the amendments made by subsections (a), (b), and (c) of this section shall also apply to public housing developed or operated pursuant to a contract between the Secretary of Housing and Urban Development and an Indian housing authority.

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**PUBLIC ANNOUNCEMENT OF HUD FUNDING DECISIONS
AND HOUSING ASSISTANCE ALLOCATIONS**

SEC. 102. Section 7 of the Department of Housing and Urban Development Act is amended by adding at the end thereof the following new subsections:

"(q)(1) The Secretary shall notify the public of all funding decisions made by the Department. The notification shall include the following elements for each funding decision --

"(A) the name and address of each funding recipient;

"(B) the name or other means of identifying the project, activity, or undertaking for each funding recipient;

"(C) the dollar amount of the funding for each project, activity, or undertaking;

"(D) the citation to the statutory, regulatory, or other criteria under which the funding decision was made; and

"(E) such additional information as the Secretary deems appropriate for a clear and full understanding of the funding decision.

"(2) The notification referred to in paragraph (1) of this subsection shall be published as a Notice in the Federal Register at least quarterly.

"(3) For purposes of this subsection, the term 'funding decision' means the decision of the Secretary to

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make available grants, loans, or any other form of financial assistance to an individual or to an entity, including (but not limited to) a State or local government or agency thereof (including a public housing agency), an Indian tribe, or a nonprofit organization, under any program administered by the Department that provides, by statute, regulation, or otherwise, for the competitive distribution of financial assistance.

"(r) The Secretary shall publish a Notice in the Federal Register at least annually informing the public of the allocation of assistance under section 213(d)(1)(A) of the Housing and Community Development Act of 1974."

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PROHIBITION OF ADVANCE DISCLOSURE OF FUNDING DECISIONS

SEC. 103. The Department of Housing and Urban Development Act is amended by adding the following new section at the end thereof:

"SEC. 12. (a)(1) No employee of the Department may disclose any information concerning a funding decision of the Department to any person who is not an employee of the Executive Branch until the decision is final, except for information that is available to the public, including program requirements and timing of the decision.

"(2) For purposes of this section, the term 'funding decision' means the decision of the Secretary to make available grants, loans, or any other form of financial assistance to an individual or to an entity, including (but not limited to) a State or local government or agency thereof, a public housing agency, an Indian tribe, or a nonprofit organization, under any program administered by the Department that provides, by statute, regulation, or otherwise, for the competitive distribution of financial assistance.

"(b)(1) CIVIL MONEY PENALTIES. -- Whenever any employee of the Department violates the prohibition in subsection (a)(1), the Secretary may impose a civil money penalty on the employee in accordance with the provisions of this section. This penalty shall be in addition to any other available civil remedy or any available criminal penalty,

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and may be imposed whether or not the Secretary takes other disciplinary action.

"(2) AMOUNT OF PENALTY. -- The amount of the penalty, as determined by the Secretary, may not exceed \$10,000 for each violation.

"(c)(1) PROCEDURES. -- The Secretary shall establish standards and procedures governing the imposition of civil money penalties under subsection (b). These standards and procedures --

"(A) shall provide for the Secretary to make the determination to impose a penalty or to use an administrative entity to make the determination;

"(B) shall provide for the imposition of a penalty only after the employee has been given an opportunity for a hearing on the record by a hearing officer, who shall be an Administrative Law Judge authorized by the Secretary to conduct hearings; and

"(C) may provide for review by the Secretary of any determination or order, or interlocutory ruling, arising from a hearing.

If no hearing is requested within 15 days of receipt of the notice of opportunity for hearing, the imposition of the penalty shall constitute a final and unappealable determination. If the Secretary reviews the determination or order of the Administrative Law Judge, the Secretary may affirm, modify, or reverse that determination or order. If

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the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order shall be the final determination or order of that Secretary.

"(2) FACTORS IN DETERMINING AMOUNT OF PENALTY. -- In determining the amount of a penalty under subsection (b), the Secretary or Administrative Law Judge shall take into account such factors as the gravity of the offense, any history of prior disclosures of information on pending funding decisions made after the date of enactment of this section, ability to pay the penalty, injury to the public, benefits received, deterrence of future violations, and such other factors as the Secretary may determine in regulations to be appropriate.

"(3) REVIEWABILITY OF IMPOSITION OF A PENALTY. -- The Secretary's determination or order imposing a penalty under subsection (b) shall not be subject to review, except as provided in subsection (d).

"(d)(1) JUDICIAL REVIEW OF DETERMINATION. -- After exhausting all administrative remedies established by the Secretary under subsection (c)(1), the employee against whom the Secretary has imposed a civil money penalty under subsection (b) may obtain a review of the penalty and such ancillary issues as may be addressed in the notice of determination to impose a penalty under subsection (c)(1)(A) in the court of appeals of the United States, within any circuit where the person resides or has a principal place of

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business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within 20 days after the entry of such order or determination, a written petition praying that the order or determination of the Secretary be modified or set aside in whole or in part.

"(2) **OBJECTIONS NOT RAISED IN HEARING.** -- The court shall not consider any objection that was not raised in the hearing conducted pursuant to subsection (c)(1), unless a demonstration is made of extraordinary circumstances causing the failure to raise the objection. If any party demonstrates to the satisfaction of the court that additional evidence not presented at the hearing is material and that there were reasonable grounds for the failure to present such evidence at the hearing, the court shall remand the matter to the Secretary for consideration of the additional evidence.

"(3) **SECRETARY'S ACTION CONCLUSIVE.** -- The decisions, findings, and determinations of the Secretary with respect to the questions of fact shall be conclusive, and shall not be set aside unless the court finds they are not supported by substantial evidence. In concluding whether the decisions, findings, and determinations of the Secretary are not supported by substantial evidence, the court shall review the whole record or those parts of it cited by a party, and take due account of the rule of prejudicial error.

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"(4) ORDER TO PAY PENALTY. -- Notwithstanding any other provision of law, in any such review the court shall have the power to order payment of the penalty imposed by the Secretary.

"(e) ACTION TO COLLECT THE PENALTY. -- If any employee fails to comply with the determination or order of the Secretary imposing a civil money penalty under subsection (b), after the determination or order is no longer subject to review as provided by subsections (c)(1) and (d), the Secretary may request the Attorney General of the United States to bring an action in an appropriate United States district court to obtain a monetary judgment against the employee and such other relief as may be available. The monetary judgment may, in the court's discretion, include the attorneys' fees and other expenses incurred by the United States in connection with the action. In an action under this subsection, the validity and appropriateness of the Secretary's determination or order imposing the penalty shall not be subject to review.

"(f) SETTLEMENT. -- The Secretary may compromise, modify, or remit any civil money penalty which may be, or has been, imposed under this section.

"(g) DEPOSIT OF PENALTIES. -- The Secretary shall deposit all civil money penalties collected under this section into miscellaneous receipts of the Treasury.

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"(h) REGULATIONS. -- The Secretary shall issue such regulations as that Secretary deems appropriate to implement his or her respective responsibilities under this section.

"(i) APPLICABILITY. -- This section shall apply only with respect to violations that occur on or after the date of enactment of this Act.".

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REPORT OF THE HEADQUARTERS RESERVE**SEC. 104. (a) FUNDING CATEGORIES. -- (1)**

Section 213(d)(4) of the Housing and Community Development Act of 1974 is amended to read as follows:

"(4) The Secretary is authorized, to such extent and in such amounts as may be approved in appropriation Acts, to make assistance available:

"(A) for unforeseeable housing needs resulting from natural and other disasters;

"(B) for housing needs resulting from emergencies, as certified by the Secretary, other than such disasters;

"(C) to provide assisted housing as a result of the settlement of litigation; and

"(D) in support of public housing desegregation efforts carried out by the Secretary."

(2) The amendment made by paragraph (1) shall take effect on October 1, 1990.

(b) **TRANSITION.** -- On or after the effective date of subsection (a)(1) of this section, no assistance may be made available under section 213(d)(4) of the Housing and Community Development Act of 1974, as it existed immediately before that date, except pursuant to a reservation for such assistance entered into before that date.

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(c) **APPLICABILITY.** -- Any assistance made available under section 213(d)(4) of the Housing and Community Development Act of 1974, as it existed immediately before the effective date of subsection (a)(1) of this section, shall continue to be governed by the provisions of such section 213(d)(4).

(d) **INDIAN HOUSING.** -- In accordance with section 201(b)(2) of the United States Housing Act of 1937, the amendments made by subsection (a) and the provisions of subsections (b) and (c) of this section shall also apply to public housing developed or operated pursuant to a contract between the Secretary of Housing and Urban Development and an Indian housing authority.

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REFORM OF THE CDBG DISCRETIONARY FUND; TECHNICAL ASSISTANCE**SEC. 105. (a) REFORM OF THE CDBG DISCRETIONARY**

FUND. -- (1) The section caption of section 107 of the Housing and Community Development Act of 1974 is amended to read as follows: "SPECIAL PURPOSE GRANTS".

(2) Section 107(b) of such Act is amended by striking out paragraphs (1) and (4); renumbering paragraphs (2), (3), and (5) as paragraphs (1), (2), and (4), respectively; and inserting the following new paragraph (3) after paragraph (2), as redesignated:

"(3) to historically Black colleges;".

(3) Section 107(a) of such Act is amended --

(A) in the first sentence, by striking out "in a special discretionary fund"; and

(B) by striking out the second and third sentences.

(4) On or after the effective date of this Act, no grant may be made under section 107(b)(1) or (4) of the Housing and Community Development Act of 1974, as it existed immediately before such effective date, except a grant made --

(A) pursuant to a grant award notification made before such effective date; or

(B) to the Park Central New Community Development Project from amounts appropriated for that project before such effective date, as provided by the second

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sentence of section 107(a) of Housing and Community Development Act of 1974, as such sentence existed immediately before such effective date.

(5) Any grant made under section 107(b)(1) or (4), as it existed immediately before the effective date of this Act, shall continue to be governed by the provisions of such section 107(b)(1) or (4).

(b) **AUTHORITY FOR TECHNICAL ASSISTANCE.** -- Section 7 of the Department of Housing and Urban Development Act is amended by adding the following new subsection at the end thereof:

"(s)(1) In addition to amounts otherwise appropriated, and to the extent approved in appropriation Acts, the Secretary is authorized to transfer up to 0.1 percent of amounts appropriated for the authorities set forth in paragraph (3) to any appropriate account, to provide technical assistance: Provided, That amounts for direct loans, and amounts for section 9 of the United States Housing Act of 1937, shall not be transferred unless a specific provision is made therefor in an appropriation Act.

"(2) The Secretary shall have the authority to obligate any amount transferred in accordance with paragraph (1) only (A) during the first fiscal year of availability of the appropriation from which the transfer is made, and (B) the next fiscal year. Any

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amount not obligated by the end of that next year shall be rescinded.

"(3) The authorities referred to in paragraph (1) are --

"(A) titles I and II of the United States Housing Act of 1937;

"(B) section 202 of the Housing Act of 1959;

"(C) the Fair Housing Act;

"(D) title I of the Housing and Community Development Act of 1974;

"(E) section 810 of the Housing and Community Development Act of 1974;

"(F) section 201 of the Housing and Community Development Amendments of 1978;

"(G) the Congregate Housing Services Act of 1978;

"(H) section 222 of the Housing and Urban-Rural Recovery Act of 1983;

"(I) section 561 of the Housing and Community Development Act of 1987;

"(J) title IV of the Stewart B. McKinney Homeless Assistance Act; and

"(K) section 106 of the Housing and Urban Development Act of 1968.

"(4) The Secretary may use funds derived from each authority specified in each subparagraph of

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paragraph (3) for any program under each specified authority.

"(5) No technical assistance may be made available under any authority referred to in paragraph (3) other than pursuant to this subsection, except technical assistance provided using funds appropriated for that purpose before the date of enactment of the Department of Housing and Urban Development Reform Act of 1989."

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WAIVER OF HUD REGULATION REQUIREMENTS AND HANDBOOK PROVISIONS

SEC. 106. Section 7 of the Department of Housing and Urban Development Act is amended by adding at the end thereof the following new subsection:

"(t)(1) All waivers of regulations of the Department shall be in writing and shall specify the grounds for approving the waiver.

"(2) The Secretary may delegate authority to approve a waiver of a regulation only to an individual of Assistant Secretary rank, or equivalent, who is authorized to issue the regulation to be waived.

"(3) The Secretary shall notify the public of all waivers of regulations approved by the Department. The notification shall be included in a Notice in the Federal Register published at least quarterly. Each notification shall cover the period beginning with the last Notice, and shall (A) identify the project, activity, or undertaking involved; (B) describe the nature of the requirement that has been waived and specify the provision involved; (C) specify the name and title of the official who granted the waiver request; (D) include a brief description of the grounds for approval of the waiver; and (E) state how more information about the waiver and a copy of the request and the approval may be obtained.

"(4) Waivers of handbook provisions shall be in writing, shall specify the grounds for approving the waiver,

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and shall be maintained in indexed form and made available for public inspection for at least the three-year period after the waiver.".

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**AUTHORITY FOR THE SECRETARY TO IMPOSE CIVIL MONEY
PENALTIES ON MORTGAGEES AND LENDERS**

SEC. 107. (a) Title V of the National Housing Act is amended by adding at the end thereof the following new section:

**"AUTHORITY FOR THE SECRETARY TO IMPOSE CIVIL MONEY
PENALTIES ON MORTGAGEES AND LENDERS**

"SEC. 536. (a)(1) GENERAL. -- Whenever a mortgagee approved under this Act, or a lender holding a contract of insurance under title I of this Act, violates any of the provisions of subsection (b), the Secretary may impose a civil money penalty on the mortgagee or lender in accordance with the provisions of this section. This penalty shall be in addition to any other available civil remedy or any available criminal penalty, and may be imposed whether or not the Secretary imposes other administrative sanctions.

"(2) AMOUNT OF PENALTY. -- The amount of the penalty, as determined by the Secretary, may not exceed \$5,000 for each violation, except that the maximum penalty for all violations by a particular mortgagee or lender during any one-year period shall not exceed \$1,000,000. Each violation of a provision of subsection (b)(1) shall constitute a separate violation with respect to each mortgage or loan application. In the case of a continuing violation, as determined by the Secretary, each day shall constitute a separate violation.

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"(b)(1) VIOLATIONS FOR WHICH A PENALTY MAY BE IMPOSED. -- The Secretary may impose a civil money penalty under subsection (a) for any of the following violations by a mortgagee or lender:

"(A) except where expressly permitted by statute, regulation, or contract approved by the Secretary, transfer of a mortgage insured under this Act to a mortgagee not approved by the Secretary, or transfer of a loan to a transferee that is not holding a contract of insurance under title I of this Act;

"(B) failure of a nonsupervised mortgagee, as defined by the Secretary, (i) to segregate all escrow funds received from a mortgagor for ground rents, taxes, assessments, and insurance premiums; or (ii) to deposit these funds in a special account with a depository institution whose accounts are insured by the Federal Deposit Insurance Corporation through the Bank Insurance Fund for banks and through the Savings Association Insurance Fund for savings associations, or by the National Credit Union Administration;

"(C) use of escrow funds for any purpose other than that for which they were received;

"(D) submission to the Secretary of information that the mortgagee or lender knew, or should have known, was false, in connection with any mortgage

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insured under this Act, or any loan that is covered by a contract of insurance under title I of this Act;

"(E)(i) hiring an officer, director, principal, or employee whose duties will involve, directly or indirectly, programs administered by the Secretary, when the mortgagee or lender knew, or should have known, that the person was under suspension or debarment by the Secretary; or (ii) retaining in employment an officer, director, principal, or employee who continues to be involved, directly or indirectly, in programs administered by the Secretary, when the mortgagee or lender knew, or should have known, that the person was under suspension or debarment by the Secretary;

"(F) falsely certifying to the Secretary or knowingly submitting to the Secretary a false certification by another person or entity;

"(G) failure to comply with an agreement, certification, or condition of approval set forth on, or applicable to (i) the application of a mortgagee or lender for approval by the Secretary, or (ii) the notification by a mortgagee or lender to the Secretary concerning establishment of a branch office; or

"(H) violation of any provisions of title I, II, or X (as it existed immediately before the effective date of the Department of Housing and Urban Development

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Reform Act of 1989) of this Act or any implementing regulation or mortgagee or title I letter that is issued under this Act.

"(2) NOTIFICATION TO ATTORNEY GENERAL. -- Before taking action to impose a civil money penalty for a violation under paragraph (1)(D) or (1)(F), the Secretary shall inform the Attorney General of the United States.

"(c)(1) AGENCY PROCEDURES. -- The Secretary shall establish standards and procedures governing the imposition of civil money penalties under subsection (a). These standards and procedures (A) shall provide for the Secretary to make the determination to impose the penalty or for use of an administrative entity (such as the Mortgagee Review Board, established pursuant to 24 CFR Part 25) to make the determination; (B) shall provide for the imposition of a penalty only after the mortgagee or lender has been given an opportunity for a hearing on the record by a hearing officer, who shall be an Administrative Law Judge authorized by the Secretary to conduct hearings; and (C) may provide for review by the Secretary of any determination or order, or interlocutory ruling, arising from a hearing. If no hearing is requested within 15 days of receipt of the notice of opportunity for hearing, the imposition of the penalty shall constitute a final and unappealable determination. If the Secretary reviews the determination or order of the Administrative Law Judge, the Secretary may affirm, modify,

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or reverse that determination or order. If the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order shall be the final determination or order of the Secretary.

"(2) FACTORS IN DETERMINING AMOUNT OF PENALTY. -- In determining the amount of a penalty under subsection (a), the Secretary or Administrative Law Judge shall take into account such factors as the gravity of the offense, any history of prior offenses (including those before enactment of this section), ability to pay the penalty, injury to the public, benefits received, deterrence of future violations, and such other factors as the Secretary may determine in regulations to be appropriate.

"(3) REVIEWABILITY OF IMPOSITION OF A PENALTY. -- The Secretary's determination or order imposing a penalty under subsection (a) shall not be subject to review, except as provided in subsection (d).

"(d)(1) JUDICIAL REVIEW OF AGENCY DETERMINATION. -- After exhausting all administrative remedies established by the Secretary under subsection (c)(1), a mortgagee or lender against whom the Secretary has imposed a civil money penalty under subsection (a) may obtain a review of the penalty and such ancillary issues (such as any administrative sanctions under 24 CFR Part 25) as may be addressed in the notice of determination to impose a penalty under subsection (c)(1)(A) in the court of appeals of the United States, within any

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circuit where such person resides or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within 20 days after the entry of such order or determination, a written petition praying that the order or determination of the Secretary be modified or be set aside in whole or in part.

"(2) OBJECTIONS NOT RAISED IN HEARING. -- The court shall not consider any objection that was not raised in the hearing conducted pursuant to subsection (c)(1) unless a demonstration is made of extraordinary circumstances causing the failure to raise the objection. If any party demonstrates to the satisfaction of the court that additional evidence not presented at the hearing is material and that there were reasonable grounds for the failure to present such evidence at the hearing, the court shall remand the matter to the Secretary for consideration of the additional evidence.

"(3) SECRETARY'S ACTION CONCLUSIVE. -- The decisions, findings, and determinations of the Secretary with respect to the questions of fact shall be conclusive, and shall not be set aside unless the court finds they are not supported by substantial evidence. In concluding whether the decisions, findings, and determinations of the Secretary are not supported by substantial evidence, the court shall review the whole record or those parts of it cited by a

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party, and take due account of the rule of prejudicial error.

"(4) ORDER TO PAY PENALTY. -- Notwithstanding any other provision of law, in any such review the court shall have the power to order payment of the penalty imposed by the Secretary.

"(e) ACTION TO COLLECT THE PENALTY. -- If any mortgagee or lender fails to comply with the determination or order of the Secretary imposing a civil money penalty under subsection (a), after the determination or order is no longer subject to review as provided by subsections (c)(1) and (d), the Secretary may request the Attorney General of the United States to bring an action in an appropriate United States district court to obtain a monetary judgment against the mortgagee or lender and such other relief as may be available. The monetary judgment may, in the court's discretion, include the attorneys' fees and other expenses incurred by the United States in connection with the action. In an action under this subsection, the validity and appropriateness of the Secretary's determination or order imposing the penalty shall not be subject to review.

"(f) SETTLEMENT BY THE SECRETARY. -- The Secretary may compromise, modify, or remit any civil money penalty which may be, or has been, imposed under this section.

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"(g) REGULATIONS. -- The Secretary shall issue such regulations as the Secretary deems appropriate to implement this section.

"(h) DEPOSIT OF PENALTIES. -- The Secretary shall deposit all civil money penalties collected under this section into miscellaneous receipts of the Treasury."

(b) The amendment made by subsection (a) of this section shall apply only with respect to (1) violations referred to in that amendment that occur on or after the effective date of this section, or (2) in the case of a continuing violation (as determined by the Secretary of Housing and Urban Development), any portion of a violation referred to in that amendment that occurs on or after that date.

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**AUTHORITY FOR THE SECRETARY TO IMPOSE CIVIL MONEY
PENALTIES ON MULTIFAMILY MORTGAGORS**

SEC. 108. (a) Title V of the National Housing Act is amended by adding at the end thereof the following new section:

**"AUTHORITY FOR THE SECRETARY TO IMPOSE CIVIL MONEY
PENALTIES ON MULTIFAMILY MORTGAGORS**

"SEC. 537. (a) GENERAL. The penalties set forth in this section shall be in addition to any other available civil remedy or any available criminal penalty, and may be imposed whether or not the Secretary imposes other administrative sanctions.

"(b)(1) PENALTY FOR VIOLATION OF AGREEMENT AS A CONDITION OF A TRANSFER OF PHYSICAL ASSETS, A FLEXIBLE SUBSIDY LOAN, A CAPITAL IMPROVEMENT LOAN, A MODIFICATION OF THE MORTGAGE TERMS, OR A WORK-OUT AGREEMENT. Whenever a mortgagor of property that includes five or more living units and that has a mortgage insured, co-insured, or held pursuant to the National Housing Act, which has agreed in writing, as a condition of a transfer of physical assets, a flexible subsidy loan, a capital improvement loan, a modification of the mortgage terms, or a work-out agreement, to use non-project income to make cash contributions for payments due under the note and mortgage, for payments to the reserve for replacements, to restore the project to good physical condition, or to pay other project liabilities, fails to comply with any of these commitments, the Secretary

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may impose a civil money penalty on that mortgagor in accordance with the provisions of this section.

"(2) AMOUNT OF PENALTY FOR SUBSECTION (b)

VIOLATION. -- The amount of the penalty, as determined by the Secretary, for a violation of subsection (b) may not exceed the amount of the loss the Secretary would experience at a foreclosure sale, or a sale after foreclosure, of the property involved.

"(c)(1) VIOLATIONS OF REGULATORY AGREEMENT FOR WHICH A PENALTY MAY BE IMPOSED. -- The Secretary may also impose a civil money penalty on a mortgagor of property that includes five or more living units and that has a mortgage insured, co-insured, or held pursuant to the National Housing Act for any of the following violations of the regulatory agreement executed by the mortgagor:

"(A) conveyance, transfer, or encumbrance of any of the mortgaged property, or permitting the conveyance, transfer, or encumbrance of such property, without the prior written approval of the Secretary;

"(B) assignment, transfer, disposition, or encumbrance of any personal property of the project, including rents, or paying out any funds, except for reasonable operating expenses and necessary repairs, without the prior written approval of the Secretary;

"(C) conveyance, assignment, or transfer of any beneficial interest in any trust holding title to the

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property, or the interest of any general partner in a partnership owning the property, or any right to manage or receive the rents and profits from the mortgaged property, without the prior written approval of the Secretary;

"(D) remodeling, adding to, reconstructing, or demolishing any part of the mortgaged property or subtracting from any real or personal property of the project, without the prior written approval of the Secretary;

"(E) requiring, as a condition of the occupancy or leasing of any unit in the project, any consideration or deposit other than the prepayment of the first month's rent, plus a security deposit in an amount not in excess of one month's rent, to guarantee the performance of the covenants of the lease;

"(F) not keeping any funds collected as security deposits separate and apart from all other funds of the project in a trust account, the amount of which at all times equals or exceeds the aggregate of all outstanding obligations under that account;

"(G) payment for services, supplies, or materials which exceeds \$500 and substantially exceeds the amount ordinarily paid for such services, supplies, or materials in the area where the services are rendered or the supplies or materials furnished;

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"(H) failure to maintain at any time the mortgaged property, equipment, buildings, plans, offices, apparatus, devices, books, contracts, records, documents, and other related papers (including failure to keep copies of all written contracts or other instruments which affect the mortgaged property) in reasonable condition for proper audit and for examination and inspection at any reasonable time by the Secretary or the Secretary's duly authorized agents;

"(I) failure to maintain the books and accounts of the operations of the mortgaged property and of the project in accordance with requirements prescribed by the Secretary;

"(J) failure to furnish the Secretary, within 60 days following the end of each fiscal year, with a complete annual financial report based upon an examination of the books and records of the mortgagor prepared and certified to by an independent public accountant or by a certified public accountant and certified to by an officer of the mortgagor, unless the Secretary has approved an extension of the 60-day period in writing;

"(K) at the request of the Secretary, the agents of the Secretary, the employees of the Secretary, or the attorneys of the Secretary, failure to furnish

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monthly occupancy reports or failure to provide specific answers to questions upon which information is sought relative to income, assets, liabilities, contracts, the operation and condition of the property, or the status of the insured mortgage; or

"(L) failure to make promptly all payments due under the note and mortgage, including mortgage insurance premiums, tax and insurance escrow payments, and payments to the reserve for replacements when there is adequate project income available to make such payments.

"(2) AMOUNT OF PENALTY FOR VIOLATIONS OF REGULATORY AGREEMENT PROVISIONS. -- The amount of the penalty, as determined by the Secretary, may not exceed \$25,000 for a violation of any of the subparagraphs of subsection (c)(1).

"(d)(1) AGENCY PROCEDURES. -- The Secretary shall establish standards and procedures governing the imposition of civil money penalties under subsections (b) and (c). These standards and procedures (A) shall provide for the Secretary or other department official (such as the Assistant Secretary for Housing) to make the determination to impose a penalty; (B) shall provide for the imposition of a penalty only after the mortgagor has been given an opportunity for a hearing on the record by a hearing officer, who shall be an Administrative Law Judge authorized by the Secretary to conduct hearings; and (C) may provide

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for review by the Secretary of any determination or order, or interlocutory ruling, arising from a hearing. If no hearing is requested within 15 days of receipt of the notice of opportunity for hearing, the imposition of the penalty shall constitute a final and unappealable determination. If the Secretary reviews the determination or order of the Administrative Law Judge, the Secretary may affirm, modify, or reverse that determination or order. If the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order shall be the final determination or order of the Secretary.

"(2) FACTORS IN DETERMINING AMOUNT OF PENALTY. -- In determining the amount of a penalty under subsection (b) or (c), the Secretary or Administrative Law Judge shall take into account such factors as the gravity of the offense, any history of prior offenses (including those before enactment of this section), ability to pay the penalty, injury to the public, benefits received, deterrence of future violations, and such other factors as the Secretary may determine in regulations to be appropriate.

"(3) REVIEWABILITY OF IMPOSITION OF A PENALTY. -- The Secretary's determination or order imposing a penalty under subsection (b) or (c) shall not be subject to review, except as provided in subsection (e).

"(e)(1) JUDICIAL REVIEW OF AGENCY DETERMINATION. -- After exhausting all administrative remedies established by

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the Secretary under subsection (d)(1), a mortgagor against whom the Secretary has imposed a civil money penalty under subsection (b) or (c) may obtain a review of the penalty and such ancillary issues as may be addressed in the notice of determination to impose a penalty under subsection (d)(1)(A) in the court of appeals of the United States, within any circuit where such person resides or has his, her, or its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within 20 days after the entry of such order or determination, a written petition praying that the order or determination of the Secretary be modified or be set aside in whole or in part.

"(2) OBJECTIONS NOT RAISED IN HEARING. -- The court shall not consider any objection that was not raised in the hearing conducted pursuant to subsection (d)(1) unless a demonstration is made of extraordinary circumstances causing the failure to raise the objection. If any party demonstrates to the satisfaction of the court that additional evidence not presented at such hearing is material and that there were reasonable grounds for the failure to present such evidence at the hearing, the court shall remand the matter to the Secretary for consideration of the additional evidence.

"(3) SECRETARY'S ACTION CONCLUSIVE. -- The decisions, findings, and determinations of the Secretary with respect

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to the questions of fact shall be conclusive, and shall not be set aside unless the court finds they are not supported by substantial evidence. In concluding whether the decisions, findings, and determinations of the Secretary are not supported by substantial evidence, the court shall review the whole record or those parts of it cited by a party, and shall take due account of the rule of prejudicial error.

"(4) ORDER TO PAY PENALTY. -- Notwithstanding any other provision of law, in any such review the court shall have the power to order payment of the penalty imposed by the Secretary.

"(f) ACTION TO COLLECT THE PENALTY. -- If any mortgagor fails to comply with the determination or order of the Secretary imposing a civil money penalty under subsection (b) or (c), after the determination or order is no longer subject to review as provided by subsections (d)(1) and (e), the Secretary may request the Attorney General of the United States to bring an action in an appropriate United States district court to obtain a monetary judgement against the mortgagor and such other relief as may be available. The monetary judgment may, in the court's discretion, include the attorneys' fees and other expenses incurred by the United States in connection with the action. In an action under this subsection, the validity and appropriateness of the Secretary's

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determination or order imposing the penalty shall not be subject to review.

"(g) SETTLEMENT BY THE SECRETARY. -- The Secretary may compromise, modify, or remit any civil money penalty which may be, or has been, imposed under this section.

"(h) REGULATIONS. -- The Secretary shall issue such regulations as the Secretary deems appropriate to implement this section.

"(i) DEPOSIT OF PENALTIES. -- The Secretary shall deposit all civil money penalties collected under this section into miscellaneous receipts of the Treasury."

(b) The amendment made by subsection (a) of this section shall apply only with respect to violations referred to in that amendment that occur on or after the effective date of this section.

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**AUTHORITY FOR THE SECRETARY TO IMPOSE
CIVIL MONEY PENALTIES ON SECTION 202 MORTGAGORS**

SEC. 109. (a) Title II of the Housing Act of 1959 is amended by adding the following new section after section 202:

***AUTHORITY FOR THE SECRETARY TO IMPOSE CIVIL MONEY PENALTIES
ON SECTION 202 MORTGAGORS**

***SEC. 202a. (a) GENERAL.** The penalties set forth in this section shall be in addition to any other available civil remedy or any available criminal penalty, and may be imposed whether or not the Secretary imposes other administrative sanctions.

***(b)(1) PENALTY FOR VIOLATION OF AGREEMENT AS A CONDITION OF A TRANSFER OF PHYSICAL ASSETS, A FLEXIBLE SUBSIDY LOAN, A CAPITAL IMPROVEMENT LOAN, A MODIFICATION OF THE MORTGAGE TERMS, OR A WORK-OUT AGREEMENT.** Whenever a mortgagor of property that includes five or more living units and that has a mortgage held pursuant to section 202 of the Housing Act of 1959, which has agreed in writing, as a condition of a transfer of physical assets, a flexible subsidy loan, a capital improvement loan, a modification of the mortgage terms, or a work-out agreement, to use non-project income to make cash contributions for payments due under the note and mortgage, for payments to the reserve for replacements, to restore the project to good physical condition, or to pay other project liabilities, fails to

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comply with any of these commitments, the Secretary may impose a civil money penalty on that mortgagor in accordance with the provisions of this section.

"(2) AMOUNT OF PENALTY FOR SUBSECTION (b) VIOLATION. -- The amount of the penalty, as determined by the Secretary, for a violation of subsection (b) may not exceed the amount of the loss the Secretary would experience at a foreclosure sale, or a sale after foreclosure, of the property involved.

"(c)(1) VIOLATIONS OF REGULATORY AGREEMENT FOR WHICH A PENALTY MAY BE IMPOSED. -- The Secretary may also impose a civil money penalty on a mortgagor of property that includes five or more living units and that has a mortgage held pursuant to section 202 of the Housing Act of 1959 for any of the following violations of the regulatory agreement executed by the mortgagor:

"(A) conveyance, transfer, or encumbrance of any of the mortgaged property, or permitting the conveyance, transfer, or encumbrance of such property, without the prior written approval of the Secretary;

"(B) assignment, transfer, disposition, or encumbrance of any personal property of the project, including rents, or paying out any funds, except for reasonable operating expenses and necessary repairs, without the prior written approval of the Secretary;

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"(C) conveyance, assignment, or transfer of any beneficial interest in any trust holding title to the property, or any right to manage or receive the rents and any other income from the mortgaged property, without the prior written approval of the Secretary;

"(D) remodeling, adding to, reconstructing, or demolishing any part of the mortgaged property or subtracting from any real or personal property of the project, without the prior written approval of the Secretary;

"(E) requiring, as a condition of the occupancy or leasing of any unit in the project, any consideration or deposit other than the prepayment of the first month's rent, plus a security deposit in an amount not in excess of one month's rent, to guarantee the performance of the covenants of the lease;

"(F) not keeping any funds collected as security deposits separate and apart from all other funds of the project in a trust account, the amount of which at all times equals or exceeds the aggregate of all outstanding obligations under that account;

"(G) payment for services, supplies, or materials which exceeds \$500 and substantially exceeds the amount ordinarily paid for such services, supplies, or materials in the area where the services are rendered or the supplies or materials furnished;

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"(H) failure to maintain at any time the mortgaged property, equipment, buildings, plans, offices, apparatus, devices, books, contracts, records, documents, and other related papers (including failure to keep copies of all written contracts or other instruments which affect the mortgaged property) in reasonable condition for proper audit and for examination and inspection at any reasonable time by the Secretary or the Secretary's duly authorized agents;

"(I) failure to maintain the books and accounts of the operations of the mortgaged property and of the project in accordance with requirements prescribed by the Secretary;

"(J) failure to furnish the Secretary, within 60 days following the end of each fiscal year, with a complete annual financial report based upon an examination of the books and records of the mortgagor prepared and certified to by an independent public accountant or a certified public accountant and certified to by an officer of the mortgagor, unless the Secretary has approved an extension of the 60-day period in writing;

"(K) at the request of the Secretary, the agents of the Secretary, the employees of the Secretary, or the attorneys of the Secretary, failure to furnish

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monthly occupancy reports or failure to provide specific answers to questions upon which information is sought relative to income, assets, liabilities, contracts, the operation and condition of the property, or the status of the direct loan;

"(L) failure to make promptly all payments due under the note and mortgage, including tax and insurance escrow payments, and payments to the reserve for replacements when there is adequate project income available to make such payments; or

"(M) amending its articles of incorporation or by-laws, other than as permitted under the terms of the articles of incorporation approved by the Secretary, without the prior written approval of the Secretary.

"(2) AMOUNT OF PENALTY FOR VIOLATIONS OF REGULATORY AGREEMENT PROVISIONS. -- The amount of the penalty, as determined by the Secretary, may not exceed \$25,000 for a violation of any of the subparagraphs of subsection (c)(1).

"(d)(1) AGENCY PROCEDURES. -- The Secretary shall establish standards and procedures governing the imposition of civil money penalties under subsections (b) and (c). These standards and procedures (A) shall provide for the Secretary or other department official (such as the Assistant Secretary for Housing) to make the determination to impose a penalty; (B) shall provide for the imposition of a penalty only after the mortgagor has been given an

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opportunity for a hearing on the record by a hearing officer, who shall be an Administrative Law Judge authorized by the Secretary to conduct hearings; and (C) may provide for review by the Secretary of any determination or order, or interlocutory ruling, arising from a hearing. If no hearing is requested within 15 days of receipt of the notice of opportunity for hearing, the imposition of the penalty shall constitute a final and unappealable determination. If the Secretary reviews the determination or order of the Administrative Law Judge, the Secretary may affirm, modify, or reverse that determination or order. If the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order shall be the final determination or order of the Secretary.

"(2) FACTORS IN DETERMINING AMOUNT OF PENALTY. -- In determining the amount of a penalty under subsection (b) or (c), the Secretary or Administrative Law Judge shall take into account such factors as the gravity of the offense, any history of prior offenses (including those before enactment of this section), ability to pay the penalty, injury to the public, benefits received, deterrence of future violations, and such other factors as the Secretary may determine in regulations to be appropriate.

"(3) REVIEWABILITY OF IMPOSITION OF A PENALTY. -- The Secretary's determination or order imposing a penalty under

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subsection (b) or (c) shall not be subject to review, except as provided in subsection (e).

"(e)(1) JUDICIAL REVIEW OF AGENCY DETERMINATION. -- After exhausting all administrative remedies established by the Secretary under subsection (d)(1), a mortgagor against whom the Secretary has imposed a civil money penalty under subsection (b) or (c) may obtain a review of the penalty and such ancillary issues as may be addressed in the notice of determination to impose a penalty under subsection (d)(1)(A) in the court of appeals of the United States, within any circuit where the mortgagor has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within 20 days after the entry of such order or determination, a written petition praying that the order or determination of the Secretary be modified or be set aside in whole or in part.

"(2) OBJECTIONS NOT RAISED IN HEARING. -- The court shall not consider any objection that was not raised in the hearing conducted pursuant to subsection (d)(1) unless a demonstration is made of extraordinary circumstances causing the failure to raise the objection. If any party demonstrates to the satisfaction of the court that additional evidence not presented at such hearing is material and that there were reasonable grounds for the failure to present such evidence at the hearing, the court

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shall remand the matter to the Secretary for consideration of the additional evidence.

"(3) SECRETARY'S ACTION CONCLUSIVE. -- The decisions, findings, and determinations of the Secretary with respect to the questions of fact shall be conclusive, and shall not be set aside unless the court finds they are not supported by substantial evidence. In concluding whether the decisions, findings, and determinations of the Secretary are not supported by substantial evidence, the court shall review the whole record or those parts of it cited by a party, and shall take due account of the rule of prejudicial error.

"(4) ORDER TO PAY PENALTY. -- Notwithstanding any other provision of law, in any such review the court shall have the power to order payment of the penalty imposed by the Secretary.

"(f) ACTION TO COLLECT THE PENALTY. -- If any mortgagor fails to comply with the determination or order of the Secretary imposing a civil money penalty under subsection (b) or (c), after the determination or order is no longer subject to review as provided by subsections (d)(1) and (e), the Secretary may request the Attorney General of the United States to bring an action in an appropriate United States district court to obtain a monetary judgement against the mortgagor and such other relief as may be available. The monetary judgment may, in

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the court's discretion, include the attorneys' fees and other expenses incurred by the United States in connection with the action. In an action under this subsection, the validity and appropriateness of the Secretary's determination or order imposing the penalty shall not be subject to review.

"(g) SETTLEMENT BY THE SECRETARY. -- The Secretary may compromise, modify, or remit any civil money penalty which may be, or has been, imposed under this section.

"(h) REGULATIONS. -- The Secretary shall issue such regulations as the Secretary deems appropriate to implement this section.

"(i) DEPOSIT OF PENALTIES. -- The Secretary shall deposit all civil money penalties collected under this section into miscellaneous receipts of the Treasury."

(b) The amendment made by subsection(a) of this section shall apply only with respect to violations referred to in that amendment that occur on or after the effective date of this section.

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**AUTHORITY OF THE SECRETARY TO IMPOSE CIVIL MONEY
PENALTIES ON GAMA ISSUERS**

SEC. 110. (a) Title III of the National Housing Act is amended by adding at the end thereof the following new section:

**"AUTHORITY FOR THE SECRETARY TO IMPOSE CIVIL MONEY
PENALTIES ON ISSUERS**

"SEC. 317. (a)(1) GENERAL. -- Whenever an issuer or custodian approved under section 306(g) of this title violates any provisions of subsection (b), the Secretary of Housing and Urban Development may impose a civil money penalty on the issuer or the custodian in accordance with the provisions of this section. This penalty shall be in addition to any other available civil remedy or any available criminal penalty and may be imposed whether or not the Secretary imposes other administrative sanctions.

"(2) AMOUNT OF PENALTY. -- The amount of the penalty, as determined by the Secretary, may not exceed \$5,000 for each violation, except that the maximum penalty for all violations by a particular issuer or custodian during any one-year period shall not exceed \$1,000,000. Each violation of a provision of subsection (b)(1) shall constitute a separate violation with respect to each pool of mortgages. In the case of a continuing violation, as determined by the Secretary, each day shall constitute a separate violation.

"(b)(1) VIOLATIONS FOR WHICH A PENALTY MAY BE IMPOSED. -- The Secretary may impose a civil money penalty

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under subsection (a) for any of the following violations by an issuer or a custodian, as applicable:

"(A) failure to make timely payments of principal and interest to holders of securities guaranteed under section 306(g) of this title;

"(B) failure to segregate cash flow from pooled mortgages or to deposit either principal and interest funds or escrow funds into special accounts with a depository institution whose accounts are insured by the National Credit Union Administration or by the Federal Deposit Insurance Corporation through the Bank Insurance Fund for banks or through the Savings Association Insurance Fund for savings associations;

"(C) use of escrow funds for any purpose other than that for which they were received;

"(D) transfer of servicing for a pool of mortgages to an issuer not approved under this title, unless expressly permitted by statute, regulation, or contract approved by the Secretary;

"(E) failure to maintain a minimum net worth in accordance with requirements prescribed by the Association;

"(F) failure to promptly notify the Association in writing of any changes that materially affect an issuer's business status;

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"(G) submission to the Association of information that an issuer or custodian knew, or should have known, was false in connection with any securities guaranteed, or mortgages pooled, under section 306(g) of this title;

"(H) hiring, or retaining in employment, an officer, director, principal, or employee whose duties involve, directly or indirectly, programs administered by the Association when the issuer or custodian knew, or should have known, that the person was under suspension or debarment by the Secretary;

"(I) submission to the Association of a false certification either on its own behalf or on behalf of another person or entity;

"(J) failure to comply with an agreement, certification, or condition of approval set forth on, or applicable to, the application for approval as an issuer of securities under section 306(g) of this title; or

"(K) violation of any provisions of this title or any implementing regulation, handbook, or participant letter issued under authority of this title.

"(2) NOTIFICATION TO ATTORNEY GENERAL. -- Before taking action to impose a civil money penalty for a violation under paragraph (1)(G) or paragraph (1)(I), the

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Secretary shall inform the Attorney General of the United States.

"(c)(1) AGENCY PROCEDURES. -- The Secretary shall establish standards and procedures governing the imposition of civil money penalties under subsection (a). These standards and procedures (A) shall provide for the Secretary to make the determination to impose the penalty; (B) shall provide for the imposition of a penalty only after an issuer or a custodian has been given notice of, and opportunity for, a hearing on the record by a hearing officer who shall be an Administrative Law Judge authorized by the Secretary to conduct hearings; and (C) may provide for review by the Secretary of any determination or order, or interlocutory ruling, arising from a hearing. If no hearing is requested within 15 days of receipt of a notice of opportunity for hearing, the imposition of a penalty shall constitute a final and unappealable order. If the Secretary reviews the determination or order of the Administrative Law Judge, the Secretary may affirm, modify, or reverse that determination or order. If the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order shall be the final determination or order of the Secretary.

"(2) FACTORS IN DETERMINING AMOUNT OF PENALTY. -- In determining the amount of a penalty under subsection (a), the Secretary or Administrative Law Judge shall take into

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account such factors as the gravity of the offense, any history of prior offenses (including those before enactment of this section), ability to pay the penalty, injury to the public, benefits received, deterrence of future violations, and such other factors as the Secretary may determine by regulations.

"(3) REVIEWABILITY OF IMPOSITION OF A PENALTY. -- The Secretary's determination or order imposing a penalty under subsection (a) shall not be subject to review, except as provided in subsection (d).

"(d)(1) JUDICIAL REVIEW OF AGENCY DETERMINATION. -- After exhausting all administrative remedies established by the Secretary under subsection (c)(1), an issuer or a custodian against which the Secretary has imposed a civil money penalty under subsection (a) may obtain a review of the penalty, and such ancillary issues as may be addressed in the notice provided under subsection (c)(1)(A) of determination to impose a penalty, in a United States court of appeals within any circuit where such person resides or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within 20 days after the entry of such order or determination, a written petition praying that the order or determination of the Secretary be modified or be set aside in whole or in part.

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"(2) OBJECTIONS NOT RAISED IN HEARING. -- A court shall not consider any objection that was not raised in the hearing conducted pursuant to subsection (c)(1) unless a demonstration is made of extraordinary circumstances causing the failure to raise the objection. If any party demonstrates to the satisfaction of the court that additional evidence, which was not presented at such hearing, is material and that there were reasonable grounds for the failure to present such evidence at the hearing, the court shall remand the matter to the Secretary for consideration of the additional evidence.

"(3) SECRETARY'S ACTION CONCLUSIVE. -- The decisions, findings, and determinations of the Secretary with respect to the questions of fact shall be conclusive and shall not be set aside unless the court finds they are not supported by substantial evidence. In concluding whether the decisions, findings, and determinations of the Secretary are not supported by substantial evidence, the court shall review the whole record, or those parts of it cited by a party, and take due account of the rule of prejudicial error.

"(4) ORDER TO PAY PENALTY. -- Notwithstanding any other provision of law, in any such review the court shall have the power to order payment of the penalty imposed by the Secretary.

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"(e) ACTION TO COLLECT THE PENALTY. -- If any issuer or custodian fails to comply with the determination or order of the Secretary imposing a civil money penalty under subsection (a), after the determination or order is no longer subject to review as provided by subsections (c)(1) and (d), the Secretary may request the Attorney General of the United States to bring an action in an appropriate United States district court to obtain a monetary judgment against the issuer or custodian and such other relief as may be available. The monetary judgment may, in the court's discretion, include the attorneys' fees and other expenses incurred by the United States in connection with the action. In an action under this subsection, the validity and appropriateness of the Secretary's determination or order imposing the penalty shall not be subject to review.

"(f) SETTLEMENT BY THE SECRETARY. -- The Secretary may compromise, modify, or remit any civil money penalty which may be, or has been, imposed under this section.

"(g) REGULATIONS. -- The Secretary shall issue such regulations as the Secretary deems appropriate to implement this section.

"(h) DEPOSIT OF PENALTIES. -- The Secretary shall deposit all civil money penalties collected under this section into miscellaneous receipts of the Treasury."

(b) The amendment made by subsection (a) of this section shall apply only with respect to:

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(1) violations referred to in that amendment that occur on or after the effective date of this section, or

(2) in the case of a continuing violation (as determined by the Secretary of Housing and Urban Development), any portion of a violation referred to in that amendment that occurs on or after that date.

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**AUTHORITY FOR THE SECRETARY TO IMPOSE CIVIL MONEY
PENALTIES FOR VIOLATIONS OF THE INTERSTATE LAND
SALES FULL DISCLOSURE ACT**

SEC. 111. (a) The Interstate Land Sales Full Disclosure Act is amended by revising section 1423 to read as follows:

***AUTHORITY FOR THE SECRETARY TO IMPOSE CIVIL MONEY PENALTIES**

"SEC. 1423. (a)(1) GENERAL. -- Whenever any person violates any of the provisions of this title or any rule, regulation, or order issued under this title, the Secretary may impose a civil money penalty on such person in accordance with the provisions of this section. This penalty shall be in addition to any other available civil remedy or any available criminal penalty, and may be imposed whether or not the Secretary imposes other administrative sanctions.

"(2) AMOUNT OF PENALTY. -- The amount of the penalty, as determined by the Secretary, may not exceed \$1,000 for each violation, except that the maximum penalty for all violations by a particular person during any one-year period shall not exceed \$1,000,000. Each violation of this title, or any rule, regulation, or order issued under it, shall constitute a separate violation with respect to each sale or lease or offer to sell or lease. In the case of a continuing violation, as determined by the Secretary, each day shall constitute a separate violation.

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"(b)(1) AGENCY PROCEDURES. -- The Secretary shall establish standards and procedures governing the imposition of civil money penalties under subsection (a). These standards and procedures (A) shall provide for the imposition of a penalty by the Secretary only after a person has been given an opportunity for a hearing on the record by a hearing officer, who shall be an Administrative Law Judge authorized by the Secretary to conduct hearings; and (B) may provide for review of any determination or order, or interlocutory ruling, arising from a hearing. If no hearing is requested within 15 days of receipt of the notice of opportunity for hearing, the imposition of the penalty shall constitute a final and unappealable order. If the Secretary reviews the determination or order of the Administrative Law Judge, the Secretary may affirm, modify, or reverse that determination or order. If the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order shall be the final determination or order of the Secretary.

"(2) FACTORS IN DETERMINING AMOUNT OF PENALTY. -- In determining the amount of a penalty under subsection (a), the Secretary or Administrative Law Judge shall take into account such factors as the gravity of the offense, any history of prior offenses (including those before enactment of this section), ability to pay the penalty, injury to the public, benefits received, deterrence of future violations,

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and such other factors as the Secretary may determine in regulations to be appropriate.

"(3) REVIEWABILITY OF IMPOSITION OF A PENALTY. -- The Secretary's determination or order imposing a penalty under subsection (a) shall not be subject to review, except as provided in subsection (c).

"(c)(1) JUDICIAL REVIEW OF AGENCY DETERMINATION. -- After exhausting all administrative remedies established by the Secretary under subsection (b)(1), a person aggrieved by a final order of the Secretary assessing a penalty under this section may seek judicial review pursuant to section 1411.

"(2) ORDER TO PAY PENALTY. -- Notwithstanding any other provision of law, in any such review, the court shall have the power to order payment of the penalty imposed by the Secretary.

"(d) ACTION TO COLLECT THE PENALTY. -- If any person fails to comply with the determination or order of the Secretary imposing a civil money penalty under subsection (a), after the determination or order is no longer subject to review as provided by subsections (b) and (c), the Secretary may request the Attorney General of the United States to bring an action in an appropriate United States district court to obtain a monetary judgment against the person and such other relief as may be available. The monetary judgment may, in the court's discretion, include

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the attorneys' fees and other expenses incurred by the United States in connection with the action. In an action under this subsection, the validity and appropriateness of the Secretary's determination or order imposing the penalty shall not be subject to review.

"(e) SETTLEMENT BY THE SECRETARY. -- The Secretary may compromise, modify, or remit any civil money penalty which may be, or has been, imposed under this section.

"(f) REGULATIONS. -- The Secretary shall issue such regulations as the Secretary deems appropriate to implement this section.

"(g) DEPOSIT OF PENALTIES. -- The Secretary shall deposit all civil money penalties collected under this section into miscellaneous receipts of the Treasury.

(b) The amendment made by subsection (a) of this section shall apply only with respect to (1) violations referred to in that amendment that occur on or after the effective date of this section, or (2) in the case of a continuing violation (as determined by the Secretary of Housing and Urban Development), any portion of violation referred to in that amendment that occurs on or after that date.

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CONSULTANT REPORTS

SEC. 112. The Department of Housing and Urban Development Act is amended by adding the following new section:

"SEC. 13. (a) RECORD OF EXPENDITURES. -- (1) Any person who makes an expenditure to influence the decision of any officer or employee of the Department with respect to--

"(A) any assistance within the jurisdiction of the Department; or

"(B) any management action involving any assistance within the jurisdiction of the Department that has been, or is planned to be, taken, or is under consideration, including any administrative sanction, recovery or conditioning of assistance, abatement of rents in whole or in part, determination of default, or any other measure affecting any person, shall keep records, as required by this section. Such person shall keep a detailed and exact account of --

"(i) all such expenditures made by or on behalf of such person; and

"(ii) the name and address of every person to whom any such expenditure is made and the date of the expenditure.

"(2) Each person making such an expenditure shall obtain a bill, stating the particulars, for every such expenditure, and shall retain all records required by this

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whose interest the registrant appears or works and the duration of the appearance or work, the total amount the registrant is paid and is to be paid, and by whom the registrant is paid or is to be paid. Each registrant shall, between the first and tenth day of each Federal fiscal year, so long as the activity continues, file with the Secretary a detailed report of all money received and expended by the registrant during the preceding fiscal year in carrying out the work; to whom paid; and for what purposes.

"(2) The Secretary shall compile all registration information as soon as practicable after the close of the Federal fiscal year with respect to which the information is filed and shall publish it annually as a Notice in the Federal Register.

"(d) DEDUCTION OF EXPENDITURES. -- The Secretary may reduce the amount of any assistance within the jurisdiction of the Department (including the amount otherwise eligible for mortgage insurance under the National Housing Act), by the amount of any expenditures reported under subsection (b) with respect to such assistance. With respect to a management action described in subsection (a)(1)(B), the Secretary may take into account any expenditures reported under subsection (b) with respect to such action.

"(e)(1) CIVIL MONEY PENALTIES. -- Whenever any person fails to file a report under subsection (b), or any person fails to register and file a report under subsection (c),

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the Secretary may impose a civil money penalty on that person in accordance with the provisions of this section. This penalty shall be in addition to any other available civil remedy or any available criminal penalty, and may be imposed whether or not the Secretary imposes other administrative sanctions.

"(2) AMOUNT OF PENALTY. -- The amount of the penalty, as determined by the Secretary, may not exceed \$10,000 for each violation.

"(f)(1) AGENCY PROCEDURES. -- The Secretary shall establish standards and procedures governing the imposition of civil money penalties under subsection (e). These standards and procedures (A) shall provide for the Secretary to make the determination to impose the penalty or to use an administrative entity to make the determination; (B) shall provide for the imposition of a penalty only after the person has been given an opportunity for a hearing on the record by a hearing officer, who shall be an Administrative Law Judge authorized by the Secretary to conduct hearings; and (C) may provide for review by the Secretary of any determination or order, or interlocutory ruling, arising from a hearing. If no hearing is requested within 15 days of receipt of the notice of opportunity for hearing, the imposition of the penalty shall constitute a final and unappealable determination. If the Secretary reviews the determination or order of the Administrative Law Judge, the

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Secretary may affirm, modify, or reverse that determination or order. If the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order shall be the final determination or order of the Secretary.

"(2) FACTORS IN DETERMINING AMOUNT OF PENALTY. -- In determining the amount of a penalty under subsection (e), the Secretary or Administrative Law Judge shall take into account such factors as the gravity of the offense, ability to pay the penalty, injury to the public, benefits received, deterrence of future violations, and such other factors as the Secretary may determine in regulations to be appropriate.

"(3) REVIEWABILITY OF IMPOSITION OF A PENALTY. -- The Secretary's determination or order imposing a penalty under subsection (e) shall not be subject to review, except as provided in subsection (g).

"(g)(1) JUDICIAL REVIEW OF AGENCY DETERMINATION. -- After exhausting all administrative remedies established by the Secretary under subsection (f)(1), a person against whom the Secretary has imposed a civil money penalty under subsection (e) may obtain a review of the penalty and such ancillary issues as may be addressed in the notice of determination to impose a penalty under subsection (f)(1)(A) in the court of appeals of the United States, within any circuit where such person resides or has a principal place

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of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within 20 days after the entry of such order or determination, a written petition praying that the order or determination of the Secretary be modified or be set aside in whole or in part.

"(2) **OBJECTIONS NOT RAISED IN HEARING.** -- The court shall not consider any objection that was not raised in the hearing conducted pursuant to subsection (f)(1) unless a demonstration is made of extraordinary circumstances causing the failure to raise the objection. If any party demonstrates to the satisfaction of the court that additional evidence not presented at the hearing is material and that there were reasonable grounds for the failure to present such evidence at the hearing, the court shall remand the matter to the Secretary for consideration of such additional evidence.

"(3) **SECRETARY'S ACTION CONCLUSIVE.** -- The decisions, findings, and determinations of the Secretary with respect to the questions of fact shall be conclusive, and shall not be set aside unless the court finds that they are not supported by substantial evidence. In concluding whether the decisions, findings, and determinations of the Secretary are not supported by substantial evidence, the court shall review the whole record or those parts of it cited by a

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party, and take due account of the rule of prejudicial error.

"(4) ORDER TO PAY PENALTY. -- Notwithstanding any other provision of law, in any such review, the court shall have the power to order payment of the penalty imposed by the Secretary.

"(h) ACTION TO COLLECT THE PENALTY. -- If any person fails to comply with the determination or order of the Secretary imposing a civil money penalty under subsection (e), after the determination or order is no longer subject to review as provided by subsections (f)(1) and (g), the Secretary may request the Attorney General of the United States to bring an action in an appropriate United States district court to obtain a monetary judgment against the person and such other relief as may be available. The monetary judgment may, in the court's discretion, include the attorneys' fees and other expenses incurred by the United States in connection with the action. In an action under this subsection, the validity and appropriateness of the Secretary's determination or order imposing the penalty shall not be subject to review.

"(i) SETTLEMENT BY THE SECRETARY. -- The Secretary may compromise, modify, or remit any civil money penalty which may be, or has been, imposed under this section.

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"(j) REGULATIONS. -- The Secretary shall issue such regulations as the Secretary deems appropriate to implement subsections (e) through (i).

"(k) DEPOSIT OF PENALTIES. -- The Secretary shall deposit all civil money penalties collected under this section into miscellaneous receipts of the Treasury.

"(l) Definitions. -- For the purpose of this section --

"(1) The term 'Department' means the Department of Housing and Urban Development.

"(2) The term 'Secretary' means the Secretary of Housing and Urban Development.

"(3) The term 'person' means an individual (including a consultant, lobbyist, or lawyer), corporation, company, association, authority, firm, partnership, society, State, local government, or any other organization or group of people.

"(4) The term 'expenditure' includes a payment, distribution, loan, advance, deposit, gift of money, or anything else of value, and includes a contract, promise, or agreement, whether or not legally enforceable, to make an expenditure.

"(5) The term 'assistance within the jurisdiction of the Department' includes any contract, grant, loan, cooperative agreement, or other form of assistance,

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including the insurance or guarantee of a loan, mortgage, or pool of mortgages.

"(6) The term 'reasonable compensation' means, with respect to a regularly employed officer or employee of any person, compensation that is consistent with the normal compensation for such officer or employee for work that is not furnished, to or not furnished in cooperation with, the Department.

"(7) The term 'regularly employed' means, with respect to an officer or employee of a person requesting or receiving assistance within the jurisdiction of the Department or who is involved in a management action with respect to such assistance, an officer or employee who is employed by such person for at least 130 working days within one year immediately before the date of the submission that initiates departmental consideration of such person for receipt of such assistance, or the date of initiation of any management action.

"(n) This section shall take effect on the date specified in regulations implementing this section that are issued by the Secretary after notice and public comment. The regulations shall establish standards that include determinations of what types of activities constitute influence with respect to the decisions of the Department described in subsection (a)(1)(A) and (B).".

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TITLE II -- MANAGEMENT REFORM

APPOINTMENT OF CHIEF FINANCIAL OFFICER AND
FHA COMPTROLLER

SEC. 201. Section 4 of the Department of Housing and Urban Development Act is amended by adding at the end thereof the following new subsections:

"(e) There shall be in the Department a Chief Financial Officer, designated by the Secretary, who shall --

"(1) report to the Secretary through the Under Secretary;

"(2) be selected on the basis of demonstrated ability in financial management and financial systems development and operations;

"(3) serve as the principal advisor to the Secretary on financial management;

"(4) develop and maintain a financial management system for the Department (including accounting and related translated transaction systems, internal control systems, financial reporting systems, credit, and cash and debt management) which provides for --

"(A) development and maintenance of consistent, compatible, and useful data;

"(B) development and reporting of cost information; and

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"(C) integration of accounting and budget information;

"(5) supervise and coordinate all financial management activities and operations of the Department, including --

"(A) the development of financial management budgets;

"(B) the approval and management of financial management system design or enhancement projects;

"(C) the management of the internal control process;

"(D) the development of long-range financial management plans; and

"(E) oversight over credit and cash management, credit extension, debt servicing, debt collection and other credit management activities;

"(6) assist in the financial execution of the Department's budget in relation to actual expenditures and prepare timely performance reports for senior managers; and

"(7) issue such policies and directives as may be necessary to carry out this section.

"(f) There shall be in the Department a Federal Housing Administration Comptroller, designated by the Secretary, who shall --

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"(1) report directly to the Assistant Secretary for Housing-Federal Housing Commissioner;

"(2) conduct activities within the overall financial management systems developed and operated by the Department's Chief Financial Officer. Such activities shall include responsibility for --

"(A) the preparation of comprehensive Federal Housing Administration ('FHA') internal financial statements, including, without limitation, regional and program-by-program statements;

"(B) maintaining the FHA general ledger and subsidiary ledgers which shall be integrated into the overall general ledger of the Department;

"(C) cash reconciliation and the reconciliation of the FHA general ledger and subsidiary ledger accounts;

"(D) collections and deposits in the Treasury of all FHA receivables and all FHA disbursements;

"(E) the operation of the FHA cash, credit management, and investment systems;

"(F) conducting day-to-day FHA accounting and cash management and control functions;

"(G) oversight of the FHA planning and budget process;

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"(H) coordination of FHA's financial management systems including internal accounting controls; and

"(I) the integration of FHA program, budget, and accounting information.".

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PROGRAM EVALUATION AND MONITORING

SEC. 202. (a) Section 501 of the Housing and Urban Development Act of 1970 is amended by --

(1) in the first sentence, inserting immediately after "testing," the following: "evaluation, monitoring,";

(2) striking out the second and third sentences;

(3) inserting "(a)" immediately before the first sentence; and

(4) adding the following new subsection at the end thereof:

"(b)(1) There are authorized to be appropriated such sums as may be necessary to carry out the purposes of this title.

"(2)(A) In addition to amounts appropriated pursuant to subsection (b)(1), and to the extent approved in appropriation Acts, the Secretary is authorized to transfer up to 0.5 percent of amounts appropriated for the authorities set forth in subparagraph (C) to any appropriate account, to carry out the purposes of this title: Provided, That amounts for direct loans, and amounts for section 9 of the United States Housing Act of 1937, shall not be transferred unless a specific provision is made therefor in an appropriation Act.

"(B) The Secretary shall have the authority to obligate any amount transferred in accordance with subparagraph (A) only (i) during the first fiscal year of

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availability of the appropriation from which the transfer is made, and (ii) the next fiscal year. Any amount not obligated by the end of that next year shall be rescinded.

"(C) The authorities referred to in subparagraph (A) are --

"(i) titles I and II of the United States Housing Act of 1937;

"(ii) section 202 of the Housing Act of 1959;

"(iii) the Fair Housing Act;

"(iv) title I of the Housing and Community Development Act of 1974;

"(v) section 810 of the Housing and Community Development Act of 1974;

"(vi) section 201 of the Housing and Community Development Amendments of 1978;

"(vii) the Congregate Housing Services Act of 1978;

"(viii) section 222 of the Housing and Urban-Rural Recovery Act of 1983;

"(ix) section 561 of the Housing and Community Development Act of 1987;

"(x) title IV of the Stewart B. McKinney Homeless Assistance Act; and

"(xi) section 106 of the Housing and Urban Development Act of 1968.

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"(D) The Secretary may use funds derived from each authority specified in each clause of subparagraph (C) for any program under each specified authority.".

(b) The first sentence of section 511(d) of the Housing and Community Development Act of 1987 is amended by striking out
 ", including any program evaluations,".

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EXPEDITING HUD RULEMAKING

SEC. 203. Section 7(o) of the Department of Housing and Urban Development Act is amended by --

(1) striking out in paragraphs (2) and (3) "of continuous session of Congress" each place it occurs;

(2) striking out in the second sentence of paragraph (2)(A) "of continuous session";

(3) striking out paragraph (6) and inserting in lieu thereof the following new paragraph:

"(6) For purposes of this subsection, the term 'rule or regulation' does not include the setting of interest rates pursuant to section 235 of the National Housing Act."

**RATIFICATION OF THE USE OF NATIONAL COMPARABILITY
PROCEDURES FOR SECTION 8 RENTS**

Sec. 204. (a) The Secretary of Housing and Urban Development (the "Secretary") is authorized to use comparability studies in the implementation of section 8(c)(2) of the United States Housing Act of 1937, and the Congress hereby ratifies and declares valid the interpretation that the Secretary has accorded section 8(c)(2) of the Act in the Secretary's past and continuing use of comparability studies under section 8(c)(2)(C) of the Act as an independent limitation on the amount of rental adjustments that would otherwise result from application of the annual adjustment factors under section 8(c)(2)(A) of the Act. Where litigation has resulted in a judgment before the date of enactment of this section that is final and not appealable (including an order of settlement) and that is inconsistent with the Secretary's interpretation of section 8(c)(2) of the Act, this ratification of the interpretation of the Secretary may not be used as the basis for requiring the repayment of amounts paid by the Secretary in accordance with the judgment or for refusal by the Secretary to pay amounts required by the judgment.

(b) Section 8(c)(2)(C) of the United States Housing Act of 1937 is amended by inserting after the second sentence thereof the following two new sentences:

"The project owner may appeal the findings of a comparability study (i) within 30 days after receipt by the

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project owner of a comparability study from the Secretary or an appropriate State agency, or (ii) as to any comparability study received by the project owner before the date of enactment of the Department of Housing and Urban Development Reform Act of 1989, within 30 days of its enactment. The Secretary shall review the appeal promptly and make any appropriate adjustments. An appeal on comparability studies received before the date of enactment of the Department of Housing and Urban Development Reform Act of 1989 shall only be available to project owners with regard to comparability studies which have not already been subject to an appeal under existing procedures."

(c) The appeal procedure described under subsection (b) of this section shall be carried out by the Secretary under existing procedures for one year following enactment of this section. During that year, the Secretary shall, by notice and comment rulemaking, promulgate regulations to implement the appeal procedure for future appeals.

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**TARGETING CDBG AMOUNTS TO
PERSONS OF LOW AND MODERATE INCOME**

SEC. 205. (a) CDBG PRIMARY OBJECTIVE. -- The second sentence of section 101(c) of the Housing and Community Development Act of 1974 is amended by striking out "60" and inserting in lieu thereof "75".

(b) USE OF CDBG AMOUNTS TO BENEFIT LOW- AND MODERATE-INCOME PERSONS. -- (1) Section 104(b)(3) of such Act is amended to read as follows:

"(3)(A) in the case of grant amounts made available to severely distressed units of general local government, each activity will benefit low- and moderate-income persons, aid in the prevention or elimination of slums or blight, or meet other community development needs having a particular urgency because existing conditions pose a serious and immediate threat to the health or welfare of the community where other financial resources are not available to meet such needs; or

"(B) in the case of grant amounts made available to units of general local government other than those referred to in subparagraph (A), each activity will benefit low- and moderate-income persons;".

(2) Section 102(a) of such Act is amended by adding at the end thereof the following new paragraph:

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"(22) In the case of section 104(b)(3), the term 'severely distressed unit of general local government' means a unit of general local government --

"(A) for which a major disaster is declared, in accordance with 42 U.S.C. 5121 et seq., and that meets such other standards as the Secretary may determine; or

"(B) that meets the minimum standards established by the Secretary for determining the level of distress of units of general local government, which standards shall be based upon measures of the capacity of units of general local government to meet the needs of low- and moderate-income persons with their own resources. The standards referred to in clauses (A) and (B) of the previous sentence shall be contained in a regulation promulgated by the Secretary after notice and opportunity to comment."

(c) REQUIREMENTS FOR BENEFITING LOW- AND MODERATE-INCOME PERSONS. -- Section 104 of such Act is amended by adding at the end thereof the following new subsection:

"(1) The aggregate use of funds received by a grantee under section 106 and, if applicable, as a result of a guarantee under section 108, during a period specified by the grantee of not more than three years, shall principally benefit low- and moderate-income persons in a manner that

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ensures that not less than 75 percent of such funds are used for the benefit of those persons during such period."

(d) **EXPENDITURES BENEFITING LOW- AND MODERATE-INCOME PERSONS.** -- Section 105(c) of such Act is amended by adding at the end thereof the following new paragraph:

"(4) Except as otherwise provided by paragraph (3), the percentage of the aggregate funds expended by a grantee that will be considered to benefit low- and moderate-income persons for purposes of meeting the requirements of section 104(1) shall equal the proportion of the aggregate funds expended on all activities assisted under this title that is the sum of amounts determined by multiplying the percentage of the beneficiaries of each assisted activity that are low- and moderate-income persons by the amount of funds under this title that are spent on the activity."

(e) **TRANSITION PROVISION.** -- (1) The amendments made by subsections (a) through (d) of this section shall take effect upon the enactment of this Act.

(2) Any grantee that, upon receipt of the next grant following the enactment of this Act, has not completed the time period that it specified in its last certification under section 104(b)(3) of the Housing and Community Development Act of 1974, as that section existed immediately before such date of enactment, shall, at the option of the grantee --

(A) begin a new time period, as provided by the amendment made by subsection (c) of this section; or

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(B) continue to be governed by the time period that it specified under such section 104(b)(3).

The provisions of subsections (a) through (d) of this section shall apply to either option.

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CDBG ANTIPOVERTY STRATEGY

SEC. 206. (a) ANTIPOVERTY PLAN. Section 104 of the Housing and Community Development Act of 1974 is amended by --

(1) redesignating subsections (e) through (k) as subsections (f) through (l); and

(2) inserting after subsection (d) the following new subsection:

"(e)(1) A grant under section 106 may be made only if the unit of general local government or State certifies that it is following an antipoverty strategy which has been approved by the Secretary and which complies with paragraph (2).

"(2) The antipoverty strategy shall --

"(A) embody a plan that provides housing, economic development, and social service resources to persons who are living in poverty and that, to the greatest extent possible, shall involve close cooperation with community-based organizations comprised of low-income persons and others who have a stake in the community and with agencies providing assistance to low-income persons;

"(B) estimate the number of people in the community or in the nonentitlement area of the State who are living in poverty, identify the principal areas and conditions in which they live, and explain the basis for this information;

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"(C)(i) identify existing facilities, resources, and public and private organizations that are or could be used to address the needs of those living in poverty, and identify public and private funding that is or could be used to address the needs of such persons; and

"(ii) in the case of States, the information required by clause (i) shall relate to facilities, resources, organizations, and funding available throughout nonentitlement areas of the State; and

"(D)(i) in the case of grants to units of general local government, set forth a strategy for the coordination of activities assisted with grants made under section 106 with the use of facilities, resources, organizations, and funding identified under subparagraph (C)(i) that is or could be used to alleviate the conditions of persons living in poverty and assist them out of poverty; or

"(ii) in the case of States, set forth a strategy for the coordination of the method of distribution of funds with the use of facilities, resources, organizations, and funding identified under subparagraph (C)(ii) to alleviate the conditions of persons living in poverty and assist them out of poverty.

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"(3) Grantees shall adopt an antipoverty strategy only after giving citizens or, as appropriate, units of general local government an opportunity to comment on a proposed strategy and taking other actions comparable to those that apply to statements of projected use of funds under subsection (a)(2) of this section.

"(4) The Secretary shall approve the strategy unless it is incomplete, the needs or conditions identified in it are plainly inconsistent with the generally available facts or data, or the strategy is plainly inappropriate to address the identified needs."

(b) CONFORMING AMENDMENTS. (1) Section 106(c)(1) of such Act is amended by --

(A) in the first sentence, striking "or (d)" and inserting in lieu thereof "(d), or (e)";

(B) in the first sentence, striking "section 104(e)" and inserting in lieu thereof "section 104(f)"; and

(C) in subparagraph (B), striking "section 104(e)" and inserting in lieu thereof "section 104(f)".

(2) Section 106(d)(3) of such act is amended by --

(A) in subparagraph (C), striking "or (d)" and inserting in lieu thereof "(d), or (e)"; and

(B) in subparagraphs (C) and (D), striking "section 104(e)" and inserting in lieu thereof "section 104(f)".

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SYNTHESIS OF BLOCK GRANT SANCTIONS

SEC. 207. (a) Section 104(f) of the Housing and Community Development Act of 1974, as redesignated by section 206 of this Act, is amended by striking the eighth sentence and inserting the following in lieu thereof:

"If, after providing a grantee a reasonable opportunity for informal consultation, the Secretary determines that the grantee is continuing to fail to satisfy standards published in regulations to measure grantee performance pursuant to the reviews and audits described in the previous sentence, the Secretary may adjust, reduce, withhold, or withdraw amounts of the annual grants made (but not yet obligated) or to be made, in accordance with the Secretary's findings under this subsection."

(b) Section 111(a) of such Act is revised by striking "shall --" and all that follows up to the period and inserting in lieu thereof: "may adjust, reduce, withhold, or withdraw amounts of the annual grants made (but not yet obligated) or to be made".

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**NULLIFICATION OF RIGHT OF REDEMPTION OF SINGLE FAMILY
MORTGAGORS UNDER SECTION 312 REHABILITATION LOAN PROGRAM**

SEC. 208. (a) Whenever with respect to a single family mortgage securing a loan under section 312 of the Housing Act of 1964, the Secretary of Housing and Urban Development or its foreclosure agent forecloses in any Federal or State court or pursuant to a power of sale in a mortgage, the purchaser at the foreclosure sale shall be entitled to receive a conveyance of title to, and possession of, the property, subject to any interests senior to the interests of the Secretary. Notwithstanding any State law to the contrary, there shall be no right of redemption (including in all instances any right to possession based upon any right of redemption) in the mortgagor or any other person subsequent to the foreclosure sale in connection with such single family mortgage. The appropriate State official or the trustee, as the case may be, shall execute and deliver a deed or other appropriate instrument conveying title to the purchaser at the foreclosure sale, consistent with applicable procedures in the jurisdiction and without regard to any such right of redemption.

(b) Whenever with respect to a single family mortgage on a property that also has a single family mortgage securing a loan under section 312 of the Housing Act of 1964, a mortgagee forecloses in any Federal or State court or pursuant to a power of sale in a mortgage, the Secretary of Housing and Urban Development, if the Secretary is purchaser at the foreclosure

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sale, shall be entitled to receive a conveyance of title to, and possession of, the property, subject to the interests senior to the interests of the mortgagee. Notwithstanding any State law to the contrary, there shall be no right of redemption (including in all instances any right to possession based upon any right of redemption) in the mortgagor or any other person subsequent to the foreclosure sale to the Secretary in connection with a property that secured a single family mortgage for a loan under section 312 of the Housing Act of 1964. The appropriate State official or the trustee, as the case may be, shall execute and deliver a deed or other appropriate instrument conveying title to the Secretary, who is the purchaser at the foreclosure sale, consistent with applicable procedures in the jurisdiction and without regard to any such right of redemption.

(c) The following actions shall be taken in order to verify title in the purchaser at the foreclosure sale:

(1) In the case of a judicial foreclosure in any Federal or State court, there shall be included in the petition and in the judgment of foreclosure a statement that the foreclosure is in accordance with this subsection and that there is no right of redemption in the mortgagor or any other person.

(2) In the case of a foreclosure pursuant to a power of sale provision in the mortgage, the statement required in paragraph (1) shall be included in the advertisement of the sale and either in the recitals of the deed or other

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appropriate instrument conveying title to the purchaser at the foreclosure sale or in an affidavit or addendum to the deed.

(d) For purposes of this section:

(1) The term "mortgage" means a deed of trust, mortgage, deed to secure debt, security agreement, or any other form of instrument under which any interest in property, real, personal, or mixed, or any interest in property, including leaseholds, life estates, reversionary interests, and any other estates under applicable State law, is conveyed in trust, mortgaged, encumbered, pledged, or otherwise rendered subject to a lien, for the purpose of securing the payment of money or the performance of an obligation.

(2) The term "single family mortgage" means a mortgage that covers property that includes a 1- to 4-family residence.

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TITLE III -- FEDERAL HOUSING ADMINISTRATION REFORM

ANNUAL AUDITED FINANCIAL STATEMENTS

SEC. 301. Title V of the National Housing Act is amended by adding the following new section at the end thereof:

ANNUAL AUDITED FINANCIAL STATEMENTS

"SEC. 538. With respect to fiscal year 1989 and each fiscal year thereafter, the Secretary shall make available to the public a financial statement of the insurance funds established under this Act that will present their financial condition on a cash and accrual basis, consistent with generally accepted accounting principles. Each financial statement shall be audited by an independent accounting firm selected by the Secretary."

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**ELIMINATION OF PRIVATE INVESTOR-OWNERS FROM THE FHA SINGLE FAMILY
MORTGAGE INSURANCE PROGRAM**

SEC. 302. (a) ELIMINATION OF PRIVATE INVESTOR OWNERS. --
Section 203(g) of the National Housing Act is amended by striking out paragraph (2) and renumbering the remaining paragraphs accordingly.

(b) RETENTION OF PUBLIC AND NONPROFIT INVESTOR OWNERS. --
Section 203(g)(2) of such Act, as redesignated by subsection (a), is amended --

(1) by adding immediately before the semicolon at the end of subparagraph (A) a comma and the following: "or any other State or local government or an agency thereof"; and

(2) by adding immediately before the semicolon at the end of subparagraph (B) a comma and the following:

"or other private nonprofit organization that is exempt from taxation under section 501(c)(3) of the Internal Revenue Code of 1986 and intends to sell or lease the mortgaged property to low- or moderate-income persons, as determined by the Secretary".

(c) APPLICABILITY. -- The amendments made by subsections (a) and (b) of this section shall apply only with respect to --

(1) mortgages insured --

(A) pursuant to a conditional commitment issued on or after the date of the enactment of this Act; or

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(B) in accordance with the direct endorsement program (24 CFR 200.163), if the approved underwriter of the mortgagee signs the appraisal report for the property on or after the date of the enactment of this Act; and

(2) the approval of substitute mortgagors, if the original mortgagor was subject to such amendments.

(d) **TRANSITION PROVISIONS.** -- Any mortgage insurance provided under title II of the National Housing Act, as it existed immediately before the date of the enactment of this Act, shall continue to be governed (to the extent applicable) by the provisions specified in subsections (a) and (b) of this section, as such provisions existed immediately before such date.

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**LIMITATION ON SECONDARY RESIDENCES IN THE FHA SINGLE FAMILY
MORTGAGE INSURANCE PROGRAM****SEC. 303. (a) LIMITATION ON SECONDARY RESIDENCES. --**

Section 203(g)(1) of the National Housing Act is amended by adding at the end thereof the following new sentences:

"In making this determination with respect to the occupancy of secondary residences, the Secretary may not permit such occupancy unless the Secretary determines that it is necessary to avoid undue hardship to the mortgagor. In no event may a secondary residence under this subsection include a vacation home, as determined by the Secretary."

(b) **APPLICABILITY.** -- The amendments made by subsection (a) of this section shall apply only with respect to --

(1) mortgages insured --

(A) pursuant to a conditional commitment issued on or after the date of the enactment of this Act; or

(B) in accordance with the direct endorsement program (24 CFR 200.163), if the approved underwriter of the mortgagee signs the appraisal report for the property on or after the date of the enactment of this Act; and

(2) the approval of substitute mortgagors, if the original mortgagor was subject to the amendments.

(c) **TRANSITION PROVISIONS.** -- Any mortgage insurance provided under title II of the National Housing Act, as it existed immediately before the date of the enactment of this Act, shall continue to be governed (to the extent applicable) by the

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provisions of section 203(g)(1) of the National Housing Act, as such provisions existed immediately before such date.

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**REQUIRE CREDIT REVIEWS OF PERSONS ACQUIRING
FHA MORTGAGED PROPERTIES FOR LIFE OF MORTGAGE**

SEC. 304. (a) Section 203(r) of the National Housing Act is amended by --

(1) revising the first sentence of subsection (r) to read as follows:

"(r) The Secretary shall take appropriate actions to reduce losses under the single family mortgage insurance programs carried out under this title.";

(2) revising paragraphs (2) and (3) to read as follows:

"(2) requiring that at least one person acquiring ownership of a one- to four-family residential property encumbered by a mortgage insured under this title be determined to be creditworthy, under standards prescribed by the Secretary, whether or not such person assumes personal liability under the mortgage (except that acquisitions by devise or descent shall not be subject to this requirement); and

"(3) in any case where personal liability under a mortgage is assumed, requiring that the original mortgagor be advised of the procedures by which he or she may be released from liability."; and

(3) inserting at the end thereof the following new sentences:

"In order to ensure full compliance with the requirements of this section, the Secretary may require

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each insured mortgage to contain a due-on-sale provision permitting the mortgagee to accelerate and require payment of the mortgage obligation. Any such due-on-sale provision shall not be subject to section 341(d)(6) of the Garn-St Germain Depository Institutions Act of 1982."

(b) **APPLICABILITY.** -- The amendments made by subsection (a) of this section shall apply only with respect to --

(1) mortgages insured --

(A) pursuant to a conditional commitment issued on or after the date of the enactment of this Act; or

(B) in accordance with the direct endorsement program (24 CFR 200.163), if the approved underwriter of the mortgagee signs the appraisal report for the property on or after the date of the enactment of this Act; and

(2) the approval of substitute mortgagors, if the original mortgagor was subject to such amendments.

(c) **TRANSITION PROVISIONS.** -- Any mortgage insurance provided under title II of the National Housing Act, as it existed immediately before the date of the enactment of this Act, shall continue to be governed (to the extent applicable) by the provisions of section 203(r) of the National Housing Act, as such provisions existed immediately before such date.

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REPEAL OF TITLE X

SEC. 305. (a) REPEAL. -- Title X of the National Housing Act is hereby repealed.

(b) APPLICABILITY. -- On or after the date of enactment of this section, no mortgage may be insured under title X, as it existed immediately before such date, except pursuant to a commitment to insure made before such date.

(c) TRANSITION. -- Any contract of insurance entered into under title X, as it existed immediately before the date of enactment of this section, shall continue to be governed by the provisions of such title X.

(d) CONFORMING AMENDMENTS. -- (1) Section 1 of the National Housing Act is amended by striking out "X," each place it appears.

(2) Section 212(a) of such Act is amended by striking out the seventh sentence.

(3) The first sentence of section 512 of such Act is amended by striking out "X,".

(4) Section 522 of such Act is amended by inserting in the first proviso after "title X of this Act" the following: ", as it existed immediately before the effective date of section 305 of the Department of Housing and Urban Development Reform Act of 1989,".

(5) Section 530 of such Act is amended by striking out "X,".

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**STREAMLINE PROPERTY DISPOSITION REQUIREMENTS FOR
UNSUBSIDIZED MULTIFAMILY HOUSING PROJECTS**

SEC. 306. (a) Section 203(a)(1)(B) of the Housing and Community Development Amendments of 1978 is amended by striking out "or vacant".

(b) Section 203(d) of such Act is amended by --

(1) striking out in paragraph (1)(B) "or are vacant (which units shall be made available for such families as soon as possible)";

(2) redesignating paragraph (2) as paragraph (3); and

(3) inserting a new paragraph (2) after paragraph (1)

to read as follows:

"(2) In the case of multifamily housing projects (other than subsidized or formerly subsidized projects) that are acquired by a purchaser other than the Secretary at foreclosure or after sale by the Secretary, enter into annual contribution contracts with public housing agencies to provide vouchers or certificates under section 8 of the United States Housing Act of 1937 to all lower income families that are eligible for such assistance and occupy units on the date the project is acquired by the purchaser. The Secretary shall take action under this paragraph only after making a determination that there is available in the area an adequate supply of habitable affordable housing for lower income families. A determination under this paragraph is final and nonreviewable."

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**PROHIBIT DEALER AND LOAN BROKER PARTICIPATION IN
ORIGINATION OF TITLE I PROPERTY IMPROVEMENT LOANS**

SEC. 307. Section 2(b) of the National Housing Act is amended by adding at the end the following new paragraphs --

"(7) No insurance shall be granted under this section to any such financial institution with respect to any obligation representing any such loan or advance of credit or purchase of such loan or advance of credit unless the financial institution certifies to the Secretary that no loan broker, as defined by the Secretary, or any other party having a financial interest in the making of the loan or advance of credit, has provided assistance to the borrower in preparing the loan application or otherwise assisted the borrower in obtaining the loan or advance of credit with regard to the financing of alterations, repairs, and improvements to existing structures or the building of new structures as authorized under clause (i) of the first sentence of section 2(a).

"(8) Notwithstanding the provisions of subsection (a) with regard to advances of credit, no insurance shall be granted under this section to any such financial institution with respect to any obligation representing an advance of credit made on or after 90 days from the enactment of the Department of Housing and Urban Development Reform Act of 1989 or the purchase of such advance of credit with regard to the financing of alterations, repairs, and improvements to existing structures or the building of new structures as

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authorized under clause (i) or the first sentence of section 2(a).".

TITLE I -- ETHICS**ALLOCATION OF HOUSING ASSISTANCE**

Section 213(d) of the Housing and Community Development Act of 1974 requires the Department to allocate assistance under certain housing assistance programs on the basis of a needs-based formula -- the so-called fair share formula. The active programs that are subject to this requirement include the section 8 Housing Assistance Payments programs, the section 202 Elderly and Handicapped Housing Loan program, and the public and Indian housing development program. Excluded from the formula's coverage are public housing operating assistance, Comprehensive Improvement Assistance, and grants under the Rental Rehabilitation program.

Under current practice, new assistance subject to "fair share" is generally allocated by the formula to the Field or Regional Office level; awards are then made to specific recipients on a purely discretionary or competitive basis. Discretionary loans and grants are also made for a number of categories in the "Headquarters Reserve" -- a funding set-aside of up to 15% of the assistance made available for the programs subject to section 213.

In recent years, some of the programs covered by section 213 have experienced widespread waste and abuse arising from allocation decisions that involved undue political interference and "influence peddling." The most egregious examples involved the section 8 Moderate Rehabilitation program. For a number of years, the Moderate Rehabilitation program was operated without objective selection and other criteria. Another area -- the Headquarters Reserve -- has never had any regulatory or other publicly articulated funding rules. Without articulated rules, these programs were prime candidates for abuse.

Section 101 of the bill is designed to place the programs subject to section 213 of the 1974 Act on a sound programmatic footing, and to prevent these abuses from occurring in the future. It would state as the governing principle that all public and Indian housing development, and all section 8 and section 202 assistance, would first have to be allocated by the fair share formula and then awarded to the recipient pursuant to a competition. Put another way, no Federal dollar could fund an assisted project, unless that dollar was provided by the fair share formula and a competition.

The non-discretionary categories in the Headquarters Reserve would be excepted from this rule. The Headquarters Reserve contains categories such as unforeseeable housing needs arising

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from natural and other disasters or the settlement of litigation. These categories involve essentially non-discretionary matters, and thus, do not share the vulnerability to abuse that would require their inclusion in the proposal. The treatment of the Headquarters Reserve is discussed more fully in section 104 of this bill.

Any competition to award housing assistance would have to be conducted pursuant to specific criteria for the selection of assistance recipients. The criteria must be contained in either a regulation promulgated by HUD after notice and public comment or to the extent authorized by law, in a notice published in the Federal Register.

This approach is designed to provide the Department with clear and articulated guidelines for awarding its housing assistance. In both cases, the guidelines would be made available to the public and the Congress, providing the "sunshine" necessary to ensure a fair process.

The Department intends to develop its selection criteria through notice and comment rule making to the greatest extent possible. The less formal Notice approach would generally be used in special circumstances, such as where the time involved in promulgating a rule would frustrate an important public purpose, where the Congress specifies a non-regulatory funding process (see section 485 of the Stewart B. McKinney Homeless Assistance Amendments Act of 1988), or where an existing regulation calls for less formal means of notifying the public of the rules for a funding competition.

The proposal would also require the Secretary to use the fair share formula to make, as determined by the Department, any assistance allocations to the smallest practicable area, consistent with the delivery of assistance through a meaningful competitive process designed to serve areas with greater needs. This part of the proposal recognizes the desirability of using both the fair share formula and competition. Under this language, the Secretary could continue the practice of conducting separate allocations of assistance for sub-programs, such as the section 8 Voucher, the section 202, and the section 8 Certificate programs. Allocations for each such sub-program would, however, be subject to the requirement that the amounts be allocated by the fair share formula, consistent with delivery of assistance through a competition designed to serve areas with greater needs.

The proposal would attempt to provide funding cycle predictability for the assisted housing programs covered by section 213 of the 1974 Act. Specifically, the Secretary would be required to take appropriate steps to ensure that the allocation of housing assistance subject to section 213 would be made with similar frequency and at similar times for each fiscal

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year. This is designed to provide funding cycles that the public can rely upon, and to eliminate ad hoc, special-interest funding rounds.

The proposal recognizes that the availability of appropriations is a central factor in the timing of funding cycles, and makes the new requirement specifically subject to appropriations-related timing considerations. The proposal would also require the Secretary to meet the new requirement, "to the maximum extent practicable." This recognizes that there may be special considerations that warrant changes in established funding cycles. Examples would include the enactment of Supplemental Appropriations Acts, amounts made available following a rescission message, or greater carryover than anticipated from a prior funding round.

The proposal would also make clear the type of assistance that is subject to the fair share formula. As noted earlier, section 213(d)(1) of the 1974 Act specifically excludes from the formula's coverage public housing operating assistance, Comprehensive Improvement Assistance, and grants under the Rental Rehabilitation program. Roughly two-fifths of the remaining housing assistance that is subject to the "fair share" is needed to provide funding for special purposes that are not capable of geographic targeting. These purposes include amendments of existing contracts; lease adjustments under section 23 of the United States Housing Act of 1937, as in effect before amendment by the 1974 Act; renewal of assistance contracts; assistance to families that would otherwise lose assistance due to the decision of the project owner to prepay the project mortgage or not to renew the assistance contract; assistance to prevent displacement or to provide replacement housing in connection with the demolition or disposition of public and Indian housing; and assistance in support of the property disposition and loan management functions of the Secretary. "Fair sharing" by the conventional, objective fair share formula criteria will not match with these geographically untargeted needs. Moreover, while loan management and property disposition functions are awarded on a needs basis, the process used does not meet traditional modes of competition open for all.

In addition, other assistance approved in appropriation Acts to be provided to target areas with greater needs, subject to competition requirements, would also not be subject to the fair share formula. Authority for the Department to target assistance to areas with greater need will give it flexibility to address otherwise unmet critical needs and priorities through a competition held on a national level. The competition would be subject to the same provisions governing competition for the award of housing assistance as for programs subject to the fair share formula (see proposed section 213(d)(5)(B)).

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Finally, the proposal would specify that the provision requiring that between 20% and 25% of amounts be allocated to nonmetropolitan areas would apply only to funds allocated by formula. Contract amendments, renewal of assistance contracts, assistance in support of the property disposition and loan management functions, and the other categories not capable of distribution by formula are largely needed in metropolitan areas. It would significantly distort the allocation process if the 20%/25% requirement were to apply to the total amount of assistance available, since it would inappropriately require a significantly higher percentage of the incremental assistance to be allocated to nonmetropolitan areas.

**PUBLIC ANNOUNCEMENT OF HUD FUNDING DECISIONS
AND HOUSING ASSISTANCE ALLOCATIONS**

Section 102 would require HUD to inform the public of all its funding decisions that involve competition among prospective recipients, as well as all its formula allocations of housing assistance under the so-called fair share formula provisions of section 213(d)(1) of the Housing and Community Development Act of 1974. With regard to the first element of the proposal, "funding decisions" would cover any grants, loans, or other form of financial assistance provided under any HUD program that provides by statute, regulation, or otherwise for the competitive distribution of the assistance.

The notification would include the following items:

- The name and address of each funding recipient;
- The name or other identifier for the project or activity funded;
- The dollar amount awarded to each funding recipient;
- The citation to the statutory, regulatory, or other criteria under which the funding decision was made; and
- Such additional information as the Secretary deems appropriate for a clear and full understanding of the funding decision.

The notification would be accomplished by publication of a Notice in the Federal Register at least quarterly. The "at least" language is intended to permit the Secretary to publish Notices at shorter intervals, for example, where an important funding round occurs shortly after the last publication.

The proposal would also require the Secretary to publish a Notice in the Federal Register at least annually informing the public of the allocations of housing assistance under the fair share formula contained in section 213(d)(1) of the Housing and Community Development Act of 1974. The report would cover the entire fair share allocation, to the smallest area for which the formula operates. The annual publication requirement corresponds to the traditional cycle for making "fair share" allocations. The Secretary would be authorized, however, to publish allocations on a more frequent basis, if the Secretary determines that such action is appropriate.

These proposals are designed to ensure that the funding award process that HUD uses for each of its programs and the "fair share" allocation process that it uses for its housing assistance programs are fair and free from improper influence. It

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accomplishes this end by inviting the public to examine relevant information about those that "win" funding competitions and receive formula allocations of housing assistance.

The "fair share" allocation proposal, when taken together with the funding decision proposal described above and the requirement of section 101 of this Act that housing assistance be awarded to specific recipients by fair share formula and competition, comprises a comprehensive approach to ensuring the fairness of HUD's housing allocations. As noted earlier, the Department typically uses the fair share formula to allocate assistance to a certain level, and then awards assistance on a discretionary basis. Under these proposals, the public would be invited to peruse the entire housing allocation process: the formula allocations as well as the funding decisions reached in the competitive element of the allocations.

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PROHIBITION OF ADVANCE DISCLOSURE OF FUNDING DECISIONS

Section 103 would prohibit disclosure of information concerning HUD funding decisions until the decision is final, except for information that is available to the public including program requirements and timing of the decision. Prohibiting the disclosure of this information would eliminate giving any unfair financial advantage derived from such information to any individual or entity with respect to a funding decision under consideration. Any HUD employee or any other employee of the executive branch who releases such information would be subject to a civil money penalty of up to \$10,000 for each violation.

This restriction against disclosure of information on funding decisions would apply only to programs administered by the Department that provide, by statute, regulation, or otherwise, for the competitive distribution of financial assistance. The purpose of this section is to assure that individuals and entities outside of the executive branch do not obtain inside information about reviews of competing proposals that would give them an opportunity to attempt to influence the decision. Recent disclosures have indicated that some HUD funding decisions have been politically motivated.

The Inspector General's audit of the Moderate Rehabilitation program revealed that, in one instance, private consultants presented copies of HUD funding documents to officials of a public housing agency (PHA) -- normally transmitted directly by HUD to the PHA -- and indicated that the funds were theirs (the consultants) to distribute. These documents should not have been in the hands of these private consultants. At the very least, access to these funding notifications provided the developers with an unfair advantage with respect to the PHA's ultimate selections. In fact, the PHA simply selected these developers and ignored the required competitive procurement procedures.

The procedures for imposing a penalty are largely based on those for the civil money penalty authority proposed for FHA lenders and mortgagees. Where the Secretary determines that a penalty should be imposed, the employee would have an opportunity for a hearing by an Administrative Law Judge. (The reference to "Secretary" includes any other department official designated by the Secretary.) After exhausting all administrative remedies, the employee could file an appeal with the appropriate court of appeals of the United States. The Secretary would deposit civil money penalties collected under this section into miscellaneous receipts of the Treasury.

REFORM OF THE HEADQUARTERS RESERVE

Section 104 would make fundamental reforms to section 213(d)(4) of the Housing and Community Development Act of 1974, the so-called "Headquarters Reserve." The Headquarters Reserve has been a source of significant programmatic waste and abuse. Currently, the Secretary is authorized to retain for use in the Reserve up to 15% of the amounts initially made available in any fiscal year under the United States Housing Act of 1937 and other housing assistance programs. This "set-aside" approach has resulted in significant amounts of funds in search of recipients.

In addition, several of the Reserve's statutory funding categories are excessively broad. The categories contained in sections 213(d)(4)(E) and (F), respectively, are among the worst offenders. They permit Reserve amounts to be used for --

- * lower income housing needs described in housing assistance plans, and
- * innovative housing programs or alternative methods for meeting lower income housing needs approved by the Secretary.

Finally, in practice, the Reserve has been used as a wholly discretionary funding vehicle. Projects were funded directly from the Central Office without competition and even without governing regulations to govern the selection of recipients.

These three aspects of the Reserve -- the "loose" money occasioned by its set-aside structure, the breadth and width of some of its funding categories, and the "fast and loose" way in which amounts from the Reserve were awarded -- have resulted in an authority that was ripe for exploitation.

The proposal would address these problems in two ways. First, it would eliminate the troublesome funding categories. Under the proposal, the reserve would only have four categories:

- Unforeseen housing needs resulting from natural and other disasters;
- Housing needs resulting from the settlement of litigation;
- Housing for the support of public housing desegregation efforts carried out by the Secretary; and
- Housing needs resulting from emergencies, as certified by the Secretary, other than disasters.

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The first two categories are based upon the existing law governing use of the Reserve. The third represents an important use of housing assistance -- to further efforts of desegregate public housing. The fourth provides needed flexibility to provide housing assistance to respond to actual emergencies. Each of these categories is directed toward specific, objective events that avoid the "catch-all" categories of the present Reserve.

Second, the proposal would replace the current "set-aside" approach with a requirement that amounts made available for the Reserve be approved in appropriation Acts. This is designed to focus the maximum "sunshine" on the Reserve. The Department would propose, and the Congress would appropriate, amounts for the Reserve. The process would be entirely above-board, with the ultimate funding levels understood by all parties: "free" money for broad categories would be replaced by specified amounts for specified purposes.

The proposal would take effect at the beginning of fiscal year 1991 -- October 1, 1990. This recognizes the fact that the appropriation process -- needed to approve amounts under the revamped Reserve -- will have been completed for FY 1990 before the proposal would receive congressional consideration.

During FY 1990, the Department intends voluntarily to limit use of the Reserve to those categories that do not involve the kinds of discretion noted above and to activities that have previous funding commitments.

Finally, the proposal would provide for the transition to the revised Reserve.

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REFORM OF THE DISCRETION FUND; TECHNICAL ASSISTANCE

Section 105 would amend the so-called "Secretary's Discretionary Fund" under section 107 of the Housing and Community Development Act of 1974 to delete the Secretary's authority to make grants for technical assistance, special projects, and new communities.

The technical assistance and special purpose categories involve highly discretionary grants for excessively broad and undefined purposes. This has made them ready candidates for programmatic waste and abuse. In addition, Congress has frequently assumed the Secretary's "discretion" under these authorities, by earmarking funding for specific activities and projects.

The Department believes that the best way to ensure the integrity of the CDBG program is to eliminate the technical assistance and special projects categories, and to provide for the objective distribution of funds for these categories via the CDBG formula. Block grant recipients would be able to use their grant funds for the types of activities covered by these categories.

The elimination of the new communities category is a technical change. Activity under the various new communities authorities is phasing out, and there is no longer any need for authority to make grants for this purpose under section 107.

No grants could be made for technical assistance or special projects after the date of enactment of this Act, except where the grant was made pursuant to grant award notifications made before that date, or to the Park Central New Community Project from amounts that have already been appropriated for that project. Grants made before the effective date of this Act would continue to be governed by the relevant provisions of section 107 as they existed before that date.

Consistent with the proposed changes, section 107's caption would be changed from the "Discretionary Fund" to "Special Purpose Grants." Section 107 would be retained for grants to Indian Tribes and the Insular Areas, and for the purposes of assisting economically disadvantaged and minority college students participating in community development work-study programs, assisting historically Black colleges, and rectifying CDBG formula miscalculations. These purposes are narrowly drawn enough to avoid the vulnerability to waste and abuse that inheres in the funding categories proposed for elimination.

The proposal would replace the technical assistance category of the Discretionary Fund with a provision permitting the Secretary to set aside up to one-tenth of one percent of the

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amounts appropriated for any fiscal year for the United States Housing Act of 1937 (other than operating subsidies under section 9 of the Act); section 202(h) of the Housing Act of 1959; the Fair Housing Act; title I of the Housing and Community Development Act of 1974; section 810 of the Housing and Community Development Act of 1974; section 201 of the Housing and Community Development Amendments of 1978; the Congregate Services Act of 1978; section 222 of the Housing and Urban-Rural Recovery Act of 1983; section 561 of the Housing and Community Development Act of 1987; title IV of the Stewart B. McKinney Homeless Assistance Act; and counseling under section 106 of the Housing and Urban Development Act of 1968.

The Secretary would be authorized to use amounts set aside for any of these authorities for the purpose of providing technical assistance in connection with that authority. The Secretary could provide the technical assistance directly, or by grants, contracts, or interagency agreement.

This proposal recognizes the legitimate purposes that are served by technical assistance. It would ensure that a small, but constant, source of funds are available for technical assistance. Rather than using the overly broad technical assistance category of the Discretionary Fund, however, the proposal would tie the technical assistance to the authority for which the assistance is to be used. The Department believes that this approach would ensure that appropriate amounts are available for technical assistance, but without the difficulties that have afflicted the current authority in the Discretionary Fund.

The proposal would ensure that technical assistance is made available only under the new authority. This would provide a single source of accountability, and eliminate disparate technical assistance authorities throughout the Department's programs. Specifically, the proposal would provide that on and after the effective date of the Department of Housing and Urban Development Reform Act of 1989, no technical assistance could be made available under any of the covered authorities other than pursuant to the proposal, except pursuant to funds appropriated for technical assistance before such date.

Finally, to ensure that all amounts set aside are used expeditiously, the proposal would provide that any amounts set aside that remain available for obligation at the end of the fiscal year after the fiscal year for which they were appropriated would be rescinded.

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WAIVER OF HUD REGULATION REQUIREMENTS AND HANDBOOK PROVISIONS

Section 106 would add a new section 7(t) to the Department of Housing and Urban Development Act governing waivers of regulations and handbooks of the Department.

Waivers provide essential flexibility in the administration of the Department's programs. In an ideal world, regulations and handbooks of an Executive Branch agency would anticipate all situations and provide enough flexibility so waivers would never be needed. As a practical matter, there are times when it is necessary to waive a generally applicable requirement. For example, unique site features, unusual local zoning laws, or urgent need for low- and moderate-income assistance could require that HUD approve a waiver of its administrative, nonstatutory requirements in order to approve a high-quality project. However, in recent months, a number of circumstances have come to light indicating the need to assure that waivers are not approved on the basis of favoritism. Problems can occur, for example, when waiver authority is abused to assist luxury projects whose excessive costs endanger the project and the FHA insurance fund.

In particular, this section would require that approval of a regulation waiver be in writing and specify the grounds for approval. To assure that regulations are waived in limited circumstances, they would have to be approved personally by the Secretary or by the Assistant Secretary or individual of equivalent rank (including the General Counsel and the President of the Government National Mortgage Association) who is authorized to issue the regulation to be waived.

Section 7(s) would also require the Department to publish a list of all approved regulation waivers as a Notice in the Federal Register on a quarterly basis. Each notification would (a) identify the project, activity, or undertaking; (b) describe the regulation to be waived; (c) identify the official approving the waiver; (d) briefly describe the grounds for approval; and (e) state how more information about the waiver and a copy of the approval may be obtained. Making regulation waiver approvals public should eliminate situations where waivers are approved for political purposes. The Department intends that waivers should be approved only where they are in the public interest or necessary to prevent undue hardship, and then only where they are consistent with the objectives of the program and the Secretary. By requiring public announcement of regulation waivers, the Department will assure that only waivers that can withstand public scrutiny under this "sunshine" initiative will be approved.

Waivers of HUD handbook provisions would also have to be in writing and specify the grounds for approving the waiver. Handbook waivers would be maintained at the Department for at

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least three years, indexed, and made available for public inspection.

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**AUTHORITY FOR THE SECRETARY TO IMPOSE CIVIL MONEY
PENALTIES ON MORTGAGEES AND LENDERS**

Section 107 would amend the National Housing Act by adding a new section 536 to authorize the Mortgagee Review Board to impose civil money penalties on HUD-approved mortgagees and title I lenders for specified violations of FHA program requirements, including: (1) transfer of a mortgage to a mortgagee not approved by HUD; (2) transfer of a title I loan to a lender that does not have a valid insurance contract with the Department; (3) failure to properly segregate or deposit escrow funds or use of these funds for a purpose other than that for which they were received; (4) submission of false information, or falsely certifying, to HUD; and (5) knowingly hiring an individual suspended or debarred from HUD programs. The penalty under this proposal would be \$5,000 per violation, with a \$1 million cap per violator for any related series of violations occurring during any one-year period. In the case of a continuing violation, each day would constitute a separate violation. There would be an opportunity for a hearing before an Administrative Law Judge, and judicial review of the Department's decision.

This amendment would permit the Secretary to more effectively deter fraud and other violations by mortgagees and lenders, thus strengthening the sanctioning process. The possibility of civil money penalties should also help expedite execution of settlement agreements.

This proposal is similar to other proposals in the bill which would authorize the imposition of civil money penalties against developers who violate the Interstate Land Sales Full Disclosure Act; against section 202 and FHA multifamily program mortgagors; and against issuers of GNMA guaranteed mortgage-backed securities and GNMA custodians.

Mortgagee Review Board

This proposal would authorize the Secretary or an administrative entity, such as the Mortgagee Review Board, to make the determination to impose the civil money penalty. (The reference to "Secretary" includes another department official.) In 1975, HUD established the Mortgagee Review Board (the Board) to act for the Secretary in determining whether to withdraw approval from mortgagees to originate mortgages because they violated certain National Housing Act requirements. See 24 CFR Part 25. From time to time, HUD has changed the structure and authority of the Board. At present, the Board has the power to take a range of administrative actions against both mortgagees and lenders. Where the Board finds that the requirements of any of the programs administered under the Act have been violated, it may: issue a letter of reprimand; place the mortgagee or lender on probation; issue an order temporarily suspending a mortgagee's

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or lender's approval; issue an order withdrawing HUD's approval of a mortgagee or title I lender to enter into a contract of insurance; or approve the initiation of a suspension or debarment action. The Board also may enter into settlement agreements with mortgagees and lenders to resolve any outstanding grounds for administrative action. These agreements may provide for monetary reimbursement to HUD for claim losses on improperly originated mortgages or title I loans that pose a risk to the FHA insurance funds. In the case of a probation, suspension, or withdrawal action, the mortgagee or lender may request a hearing before an independent hearing officer to challenge the action, and, after the hearing, any party may request review by petitioning the Secretary. In accordance with 5 U.S.C. secs. 701-706 (1988), mortgagees and lenders may secure judicial review in a United States court after they have exhausted their administrative remedies.

Background

In the past two decades, the civil money penalty has assumed a place of paramount importance in the compliance arsenal of Federal regulations. In fact, a consultant to the Informal Action Committee of the Administrative Conference of the United States wrote in 1979, "it is today almost inconceivable that Congress would authorize a major administrative regulatory program without empowering the enforcing agency to impose civil monetary penalties as a sanction." Diver, The Assessment and Mitigation of Civil Money Penalties by Federal Administrative Agencies, 79 COLUM. L. REV. 1435, at 1436 (1979).

This article pointed out that in 1979 there were 348 statutory civil penalties, enforced by 27 Federal departments and independent agencies, authorized for the enforcement of a host of regulatory commands. Civil money penalties may be invoked for violating statutes, administrative regulations, or administrative orders; for failure to file reports, keep records, permit entry, or respond to agency inquiries; or for willful, negligent, repeated, or even unintended conduct. *Id.* at 1438.

This proposal is based on a 1972 recommendation of the Administrative Conference of the United States, Civil Money Penalties as a Sanction, 1 CFR 305.72-6, that agencies consider the use of civil money penalties to supplement other civil and criminal sanctions and that, in appropriate situations, civil money penalties be imposed as part of administrative proceedings. The Conference further recommended that agencies' determinations be subject to review if not supported by substantial evidence, but not to trial *de novo* or collateral attack in a collection proceeding. This was reaffirmed by the Conference in 1979 in Agency Assessment and Mitigation of Civil Money Penalties, 1 CFR 305.79-3, and remains the position of the Conference to date. This amendment follows the format of the sample statute

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recommended by the Administrative Conference, with variations. This is in line with the Conference's recommendation that the sample statute serve as a point of departure for individual agencies' own legislation.

Need for the Amendment

Gaps in existing legislation, primarily the Program Fraud Civil Remedies Act (PFCRA) and the False Claims Act, necessitate this amendment. No penalty can be secured under the PFCRA unless there is a false statement, in the form of a certification, or a false claim. The False Claims Act also requires a false claim. In many of HUD's mortgagee/title I lender cases, however, certified false statements and false claims have not been involved. For example, one of HUD's critical loan underwriting requirements is a face-to-face meeting between the borrower and a lender representative. In many fraudulent schemes, this requirement is violated, as is the case when a straw buyer is used. The mortgagee cannot be said to have made a false claim or false statement since it does not know that a straw buyer has been used. HUD's only current remedy in such situations is to threaten, or seek to secure, sanctions against the mortgagee, up to and including withdrawal of FHA approval. The mortgagee, however, has been able to defeat such threats by terminating the individual involved or transferring ownership of the company, without suffering any financial loss itself. Thus, HUD currently cannot impose monetary penalties for violations of its regulations although such violations may be critical to causing ultimate default and loss to HUD.

Furthermore, even where there is a false statement in the form of a certification with regard to a particular loan, there would only be one \$5,000 penalty under the PFCRA (although a double damages remedy is available in the case of a false claim) because a mortgagee makes only one certification per loan to HUD. It is commonly the case, however, that mortgagees commit multiple violations with regard to a particular loan, and HUD's losses are often considerably above \$5,000. For example, HUD estimates that the average loss on a single family property is \$17,000. Under the PFCRA, HUD's recovery would be limited to \$5,000; under this amendment, HUD would be able to impose a \$5,000 penalty for each of the violations and be more apt to recover its actual losses.

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Section-by-Section Explanation

Subsection (a)(1)¹ would give the Secretary discretionary authority to impose a civil money penalty against a mortgagee or title I lender that violates the requirements set forth in subsection (b). It would make clear that the money penalty would be in addition to other available civil remedies or any available criminal penalties, and may be imposed whether or not other administrative sanctions are imposed.

Subsection (a)(2) would limit the amount of the civil money penalty to \$5,000 for each violation, except that the maximum penalty for all violations committed by a mortgagee or lender during any one-year period could not exceed \$1 million. In the case of a continuing violation, each day would constitute a separate violation. These monetary standards are similar to many other civil money penalty provisions. On September 19, 1986, Senator William Cohen placed in the Congressional Record a table listing the 200 Federal statutes then on the books authorizing enforcement through the administrative imposition of civil money penalties. These statutes included maximum penalties per violation ranging from \$5 to \$100,000 (132 CONG. REC. S13,009-11 (1986)). These 200 statutes differ from the 348 statutes referred to in the 1979 Diver article discussed in the second paragraph of the Background section above as the 348 figure included statutes which require court assessment of penalties as well as those which permit agency assessment.)

Subsections (b)(1)(A)-(G) would list the violations (already prohibited by the programs under the National Housing Act) which may warrant the imposition of civil money penalties. These violations were selected from among the numerous violations which the Board may currently sanction. The Department considers these violations to be sufficiently egregious to warrant the imposition of civil money penalties in appropriate circumstances. Subsection (b)(1)(H) would cover violations of other statutory and administrative requirements.

Subsection (b)(1)(A) would provide for the imposition of a civil money penalty when a HUD-approved mortgagee transfers a HUD-insured mortgage to a mortgagee that is not approved by the Secretary, or when a lender transfers a loan to a transferee that is not holding a contract of insurance under title I of the Act, unless the transfer is expressly permitted by statute, regulation, or contract approved by the Secretary. The National

¹ All references to subsections refer to subsections of the new section 536 of the National Housing Act, except for the reference in the last paragraph, which refers to subsection (b) of this proposed section of the bill.

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Housing Act contemplates that HUD will provide insurance only with regard to mortgagees and lenders that meet the requirements of the Act. When a mortgage or loan is transferred to a mortgagee or lender that does not meet these requirements, the Department's funds are at risk.

Paragraph (1)(B) would provide for the imposition of a civil money penalty when a mortgagee that is not supervised by the appropriate Federal, State, or local agencies (and does not, therefore, qualify as a supervised mortgagee under HUD's regulations (see, for example, 24 CFR 203.3 and 203.4)) fails to segregate all escrow funds received from a mortgagor for ground rents, taxes, assessments, and insurance premiums, or fails to deposit these funds in a special account with a depository institution whose accounts are insured by the Federal Deposit Insurance Corporation through the Bank Insurance Fund for banks and through the Savings Association Insurance Fund for savings associations, or by the National Credit Union Administration. The failure to segregate escrow funds would make accounting for these amounts difficult and could encourage the improper diversion of escrowed amounts or other illegal activity. In any event, both diversion and failure to place escrow funds in insured accounts could result in a mortgagor having to make up for lost amounts, being unable to do so, and defaulting under the mortgage.

Paragraph (1)(C) would permit the imposition of a civil money penalty when a mortgagee or lender uses escrow funds for any purpose other than that for which they were received.

Paragraph (1)(D) would permit the imposition of a civil money penalty where the mortgagee or lender knew, or should have known, that information submitted to the Secretary was false. It is vital that mortgagees and lenders provide accurate information if the Department is to avoid costly insurance claims. In implementing this paragraph, it is the intention of the Department that a mortgagee or lender would be subject to a civil money penalty if any of its employees knew, or should have known, that the information was false.

Paragraph (1)(E) would permit the Secretary to impose a civil money penalty where the mortgagee or lender hires an officer, director, principal, or employee whose duties will involve, directly or indirectly, programs administered by the Secretary, when the mortgagee or lender knew, or should have known, that the person was under suspension or debarment by the Secretary. Penalties could also be enforced where the mortgagee or lender retains in employment an officer, director, principal, or employee who continues to be involved, directly or indirectly, in programs administered by the Secretary, when the mortgagee or lender knew, or should have known, that the person was under suspension or debarment by the Secretary.

Paragraph (1)(F) would permit the Secretary to impose a civil money penalty on a mortgagee or lender that falsely certifies. The Department requires mortgagees and lenders to certify that, to the best of their knowledge, the applicable rules and regulations of the Department have been met. If the certification is false, a costly claim could result. Since mortgagees and lenders may be submitting certifications made by others, such as contractors or suppliers, paragraph (1)(F) would also permit the Secretary to impose a civil money penalty on a mortgagee or lender who knowingly submits a false certification by another person or entity.

Paragraph (1)(G) would permit the Secretary to impose a civil money penalty where the mortgagee or lender fails to comply with an agreement, certification, or condition of approval set forth (A) on, or applicable to, the application of the mortgagee or lender for approval by the Secretary, or (B) on, or applicable to, the notification from the mortgagee or lender to the Secretary that it has established a branch office. The Department's approval is conditioned on commitments by the mortgagee or lender contained on the application or notification. The mortgagee or lender would, for example, agree to submit to such examination of its records and accounts as HUD may require. Failure to comply with this and the other commitments would put the Department's insurance funds at risk.

Paragraph (1)(H) would permit the Secretary to impose a civil money penalty for the violation of any National Housing Act provision of title I, II, or X (as it existed immediately before the effective date of the Department of Housing and Urban Development Reform Act of 1989) or any implementing regulation or mortgagee or title I lender letter that is issued under the National Housing Act. Since it is not possible in legislation to cover every conceivable violation on the part of mortgagees and lenders which may occur in the future, this paragraph would give the Secretary the flexibility to impose civil money penalties for violations of the Act's other program requirements.

Subsection (b)(2) would require the Secretary to inform the Attorney General before taking action to impose a fine for a violation under paragraph (1)(D) or (1)(F).

Subsection (c)(1) would require that the Secretary establish standards and procedures governing HUD's imposition of civil money penalties under subsection (a). Under subsection (c)(1)(A), the Secretary would have the discretion to provide for the use of an administrative entity (such as the Mortgage Review Board) to make the determination to impose a penalty. In accordance with subsection (c)(1)(B), the standards and procedures would provide that the civil money penalty could not be imposed before the mortgagee or lender had an opportunity

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for a hearing on the record by an Administrative Law Judge. This differs somewhat from the procedure the Board follows with respect to probation, suspension, or withdrawal actions. A probation or suspension action by the Board becomes effective before a hearing, and the Board has discretion to determine that a withdrawal action shall also become effective before a hearing. With regard to any of these three actions, the mortgagee or lender is then entitled to a hearing within 30 days after its request. The discretion to order pre-hearing sanctions is in line with court decisions that appropriate pre-hearing sanctions do not violate due process. The courts have permitted pre-hearing sanctions where the protection of the public justifies it. With regard to the imposition of a civil money penalty, however, there is no overriding public interest which would justify imposition of the sanction before an opportunity for a hearing.

Finally, subsection (c)(1)(C) would authorize HUD to establish standards and procedures providing for review of any determination or order, or interlocutory ruling, arising from a hearing. If no hearing is requested within 15 days of receipt of the notice of opportunity for hearing, the imposition of the penalty would constitute a final and unappealable determination.

If the Secretary reviews the determination or order of the Administrative Law Judge, the Secretary may affirm, modify, or reverse that determination or order. If the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order would be the final determination or order of the Secretary.

In implementing the proposed civil money penalty authority, the Department contemplates using, to the maximum extent possible, the existing administrative sanction and review procedures in 24 CFR Parts 25 (Mortgagee Review Board) and 26 (Proceedings Before a Hearing Officer). Thus, the new authority would be coupled with a well-known, existing procedure that provides for the imposition and review of other administrative sanctions for the same types of violations.

Subsection (c)(2) would set forth the factors to be considered in determining the amount of the civil money penalty. These would consist of the gravity of the offense, any history of prior offenses (including those before enactment of this amendment), the ability of the mortgagee or lender to pay the penalty, injury to the public, benefits received, deterrence of future violations, and such other factors as the Secretary determines in regulations to be appropriate.

Subsection (d) would give mortgagees and lenders the right to judicial review in the U.S. Court of Appeals, as recommended by the Administrative Conference. The court also would have

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jurisdiction to consider any ancillary issues, such as administrative sanctions, covered by the notice of determination to impose a penalty under subsection (c). Subsection (d) would also make it clear that the reviewing court has the authority to order payment of the civil money penalty. This would avoid the possibility of the court's upholding a determination or order imposing a civil money penalty without ordering payment, which could necessitate additional litigation to secure payment. As is the existing practice with respect to other civil monetary penalties, the findings and determinations of the Secretary in imposing money penalties would not be subject to trial *de novo* by the reviewing court.

Under subsection (e), the Department could request the Attorney General to institute an action in an appropriate U.S. district court against a mortgagee or lender that fails to pay a civil money penalty after it has become a final and unappealable order. The action would seek a money judgment against the mortgagee or lender, as well as any other relief that may be available. The money judgment could include attorneys' fees and other expenses of the United States in bringing the action. The validity and appropriateness of the final order imposing the civil money penalty would not be subject to review.

Subsection (f) would give the Secretary discretion to compromise, modify, or remit any civil money penalty before or after it has been imposed. Since it is the goal of this proposal to achieve compliance with the requirements of programs administered by the Department, subsection (f) would permit the Secretary to enter into settlements which would provide for compliance, including compromise, modification, or return of any civil money penalties.

Subsection (g) would require the Secretary to issue regulations to implement the new authority.

Subsection (h) would provide that the Secretary would deposit the civil money penalties collected under this proposal into miscellaneous receipts of the Treasury.

Section 107(b) would provide that the new authority would only cover mortgagee or lender violations that occur after the effective date of the amendment. In the case of a continuing violation (as determined by HUD), the new authority would apply to any portion of the violation occurring on or after that effective date.

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**AUTHORITY FOR THE SECRETARY TO IMPOSE
CIVIL MONEY PENALTIES ON MULTIFAMILY MORTGAGORS**

Section 108(a) would amend the National Housing Act by adding a new section 537 to authorize HUD to impose civil money penalties against mortgagors of property that (1) includes five or more living units and (2) has a mortgage insured, co-insured, or held pursuant to the National Housing Act. The proposal would authorize the imposition of civil money penalties for certain violations of (A) an agreement entered into as a condition of a transfer of physical assets, a flexible subsidy loan, a capital improvement loan, a modification of the mortgage terms, or a work-out agreement; or (B) the regulatory agreement executed by the mortgagor. The penalty for violation of the agreement described in (A) above could not exceed the amount of the loss the Secretary would experience at a foreclosure sale, or a sale after foreclosure. The penalty for violation of the regulatory agreement would be capped at \$25,000 for each of the specified violations.

The violations for which civil money penalties may be imposed under section 108 were selected from among the numerous violations which the Department may currently sanction. The Department considers the violations that would be subject to a civil money penalty under this section to be sufficiently egregious to warrant the imposition of a civil money penalty in appropriate circumstances.

While the majority of mortgagors comply with their commitments, the limited sanctions presently available to the Secretary (such as declaring the mortgage in technical default for violation of the regulatory agreement, stopping subsidy payments, or foreclosing on the mortgage) have not been preventing a minority of recalcitrant mortgagors from disregarding their contractual obligations. These sanctions have a more adverse effect on the Department and the tenants than on the mortgagor. The results of the Department's declaration that a mortgage is in default are that: the Department discontinues subsidy payments, the mortgagee assigns the mortgage to the Department, the Department pays off the insurance claim, and the Department forecloses on the property at a loss. Due to these events, the project deteriorates physically and financially, with the consequent reduction in services to tenants. To avoid this, it is imperative that the Secretary have the ability to impose sanctions which are commensurate with the harm done by a recalcitrant mortgagor and which would deter mortgagors from disregarding their contractual obligations.

This amendment is similar to other civil money penalty proposals in this bill.

Need for the Legislation

Civil money penalties have proven to be an effective enforcement tool in Federal programs. Authority to impose civil money penalties for the violations involved here would provide an added incentive for mortgagors to comply with their agreements.

HUD lacks sufficient tools to assure that participants in its programs comply with program requirements. The applicable criminal penalties are often insufficient to ensure enforcement since problems of proof make criminal prosecution difficult. Authorizing the Secretary to impose civil money penalties for violations of specific program requirements will permit HUD more effectively to deter fraud and other violations under HUD programs. The possibility of civil money penalties should also help expedite execution of settlement agreements.

Gaps in existing legislation, primarily the Program Fraud Civil Remedies Act (PFCRA) and the False Claims Act, necessitate this amendment. No penalty can be secured under the PFCRA unless there is a false statement, in the form of a certification, or a false claim. The False Claims Act also requires a false claim. In many of HUD's mortgagor cases, however, certified false statements and false claims have not been involved.

Section-by-Section Analysis

Subsection (a) of proposed section 537² would make clear that the civil money penalty would be in addition to other available civil remedies or any available criminal penalties, and may be imposed whether or not other administrative sanctions are imposed.

Subsection (b)(1) would give the Secretary discretionary authority to impose a civil money penalty on any mortgagor of property that (A) has five or more living units and (B) has a mortgage insured, co-insured, or held pursuant to the National Housing Act where the mortgagor has (i) a written agreement, executed as a condition of a transfer of physical assets, a flexible subsidy loan, a capital improvement loan, a modification of the mortgage terms, or a work-out agreement, to use non-project income (ii) to make cash contributions for payments due under the note and mortgage, for payments to the reserve for replacements, to restore the project to good physical condition, or to pay other project liabilities, for failure to comply with

²All future references to subsections refer to subsections of proposed section 537 of the National Housing Act, except for the reference in the last paragraph, which refers to subsection (b) of this proposed section of this bill.

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any of these commitments. (The reference to "Secretary" includes another department official).

In most instances, where one of these agreements is executed, the Secretary agrees to provide additional subsidy resources or to forego mortgage payments for a period of time, and, in consideration of the Secretary's agreement, the mortgagor agrees to provide additional cash contributions to the project income stream to restore the project to acceptable financial and physical condition. If, after the Secretary has provided the additional resources, the owner fails to make the agreed upon cash contribution, the project will not be restored and the Department's insurance funds will be further jeopardized.

Subsection (b)(2) would limit the amount of the civil money penalty for a violation of subsection (b)(1) to the amount of the loss the Secretary would experience at a foreclosure sale, or a sale after foreclosure.

Subsection (c)(1) would give the Secretary discretionary authority to impose a civil money penalty against any mortgagor of property that (A) has five or more living units and (B) has a mortgage insured, co-insured, or held pursuant to the National Housing Act for violations of the regulatory agreement executed by the mortgagor, as specified in subparagraphs (A)-(L).

Paragraph (1)(A) would provide for the imposition of a civil money penalty for the conveyance, transfer, or encumbrance of any of the mortgaged property, or for permitting such action without the prior written approval of the Secretary.

Paragraph (1)(B) would provide for the imposition of a civil money penalty for the assignment, transfer, disposition, or encumbrance of any personal property of the project, including rents, or paying out any funds, except for reasonable operating expenses and necessary repairs, without the prior written approval of the Secretary.

Paragraph (1)(C) would provide for the imposition of a civil money penalty for the conveyance, assignment, or transfer of any beneficial interest in any trust holding title to the property, or the interest of any general partner in a partnership owning the property, or any right to manage or receive the rents and profits from the mortgaged property, without the prior written approval of the Secretary.

Paragraph (1)(D) would provide for the imposition of a civil money penalty for remodeling, adding to, reconstructing, or demolishing any part of the mortgaged property or subtracting from any real or personal property of the project, without the prior written approval of the Secretary.

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Paragraph (1)(E) would provide for the imposition of a civil money penalty where the mortgagor, as a condition of the occupancy or leasing of any unit in the project, requires any consideration or deposit other than the prepayment of the first month's rent, plus a security deposit in an amount not in excess of one month's rent, to guarantee the performance of the covenants of the lease. This paragraph is designed to protect low- and moderate-income tenants and assure equal access for all applicants.

Paragraph (1)(F) would provide for the imposition of a civil money penalty for the failure to keep any funds collected as security deposits separate and apart from all other funds of the project in a trust account, the amount of which at all times equals or exceeds the aggregate of all outstanding obligations under that account. This paragraph is designed to prevent use of the tenants' security deposits for project costs and, thus, assure the availability of these moneys when the tenants vacate the premises, provided that the premises are returned to the mortgagor in good condition.

Paragraph (1)(G) would provide for the imposition of a civil money penalty for paying over \$500 for services, supplies, or materials when such payment substantially exceeds the amount ordinarily paid for such services, supplies, or materials in the area where the services are rendered or the supplies or materials furnished. While the majority of mortgagors are cost conscious, a minority do not adequately contain costs for reasons such as the lack of professional ability to do so; the receipt of kickbacks from the provider of the services, supplies, or materials; or an identity of interest with the firm supplying the services, supplies, or materials. This has an adverse impact on tenants whose rents are set at a level to pay for these costs. It can also have an adverse impact on the Department where it provides rent subsidies, or where the overpayment contributes to an insurance claim.

Paragraph (1)(H) would provide for the imposition of a civil money penalty for failure to maintain at any time the mortgaged property, equipment, buildings, plans, offices, apparatus, devices, books, contracts, records, documents, and other related papers (including the failure to keep copies of all written contracts or other instruments which affect the mortgaged property) in reasonable condition for proper audit and for examination and inspection at any reasonable time by the Secretary or the Secretary's duly authorized agents. If the Secretary is to monitor and enforce mortgagor compliance with program requirements, it is imperative that these requirements be met.

Paragraph (1)(I) would provide for the imposition of a civil money penalty for failure to maintain the books and accounts of

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the operations of the mortgaged property and of the project in accordance with requirements prescribed by the Secretary. If the Secretary cannot impose sanctions to enforce compliance on the minority of recalcitrant mortgagors who fail to comply with this requirement, program enforcement is jeopardized since the project's cash flow is the cornerstone for maintaining the project in a good fiscal and physical condition.

Paragraph (1)(J) would provide for the imposition of a civil money penalty for failure to furnish the Secretary, within 60 days following the end of each fiscal year, with a complete annual financial report based upon an examination of the books and records of the mortgagor, prepared and certified to by an independent public accountant or a certified public accountant and certified to by an officer of the mortgagor, unless the Secretary has approved an extension of the 60-day period in writing.

Paragraph (1)(K) would provide for the imposition of a civil money penalty when, at the request of the Secretary, the agents of the Secretary, the employees of the Secretary, or the attorneys of the Secretary, the mortgagor fails to furnish monthly occupancy reports or fails to provide specific answers to questions upon which information is sought relative to income, assets, liabilities, contracts, the operation and condition of the property, or the status of the insured mortgage.

Mortgagors of financially and physically solvent projects are not required to provide the Department with monthly accountings of cash income and outlays. When the Department becomes aware, however, that a mortgagor is having financial problems with regard to a particular project, it will require the mortgagor to provide monthly accounts of income and disbursements. This is necessary to assure the proper future maintenance of the project for the benefit of the tenants and to protect the Department from claims on the insurance funds.

Paragraph (1)(L) would provide for the imposition of a civil money penalty for failure to make promptly all payments due under the note and mortgage, including mortgage insurance premiums, tax and insurance escrow payments, and payments to the reserve for replacements when there is adequate project income available to make such payments. This provision is designed to avoid having the mortgage go into default when there is adequate project income available for the required payments.

Subsection (c)(2) would cap the amount of the civil money penalty for a violation of subparagraphs (A)-(L) at \$25,000 for a violation of any of those subparagraphs. The monetary penalties that would be provided under subsection (c)(2) are similar to civil money penalties that are provided in many other Federal statutes which authorize the administrative imposition of such

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penalties. On September 19, 1986, Senator William Cohen placed in the Congressional Record a table listing the 200 Federal statutes then on the books authorizing enforcement through the administrative imposition of civil money penalties. These statutes included maximum penalties per violation ranging from \$5 to \$100,000 (132 CONG. REC. S13,009-11 (1986)).

Subsection (d)(1) would require that the Secretary establish standards and procedures governing HUD's imposition of civil money penalties under subsections (b) and (c). In accordance with subparagraph (A), the Secretary or other department official (such as the Assistant Secretary for Housing) could make the determination to impose the penalty. In accordance with subparagraph (B), the standards and procedures would provide that the civil money penalty could not be imposed before the mortgagor had an opportunity for a hearing on the record by an Administrative Law Judge. Subparagraph (C) would authorize HUD to establish standards and procedures providing for review of any determination or order, or interlocutory ruling, arising from a hearing. If a hearing is not requested within 15 days of receipt of the notice of opportunity for hearing, the imposition of the civil money penalty would be a final and unappealable determination. If the Secretary reviews the determination or order of the Administrative Law Judge, the Secretary may affirm, modify, or reverse that determination or order. If the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order would be the final determination or order of the Secretary.

In implementing the proposed civil money penalty authority, the Department contemplates using, to the maximum extent possible, the existing review procedures in 24 CFR Part 26 (Proceedings Before a Hearing Officer). Thus, the new authority would be coupled with a well-known, existing procedure.

Subsection (d)(2) would set forth factors to be considered in determining the amount of the civil money penalty. These would consist of the gravity of the offense, any history of prior offenses (including those before enactment of this proposal), the ability of the developer to pay the penalty, injury to the public, benefits received, deterrence of future violations, and such other factors as the Secretary determines in regulations to be appropriate.

Subsection (e) would give mortgagors the right to judicial review in the U.S. Court of Appeals. The court also would have jurisdiction to consider any ancillary issues, such as administrative sanctions, covered by the notice of determination to impose a penalty under subsection (d). Subsection (e) would also make it clear that the reviewing court has the authority to order payment of the civil money penalty. This would avoid the possibility of the court's upholding a determination or order

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imposing a civil money penalty without ordering payment, which could necessitate additional litigation to secure payment. As is the existing practice with respect to other civil monetary penalties, the findings and determinations of the Secretary in imposing civil money penalties would not be subject to trial de novo by the reviewing court.

Under subsection (f) the Department could request the Attorney General to institute an action in an appropriate U.S. district court against a person that fails to pay a civil money penalty after it has become a final and unappealable order. The action would seek a money judgment against the person as well as any other relief that may be available. The money judgment could include attorneys' fees and other expenses of the United States in bringing the action. The validity and appropriateness of the final order imposing the civil money penalty would not be subject to the review.

Subsection (g) would give the Secretary discretion to compromise, modify, or remit any civil money penalty before or after it has been imposed. Since it is the goal of this proposal to achieve compliance with the requirements of programs administered by the Department, subsection (g) would permit the Secretary to enter into settlements which would provide for such compliance, including compromise, modification, or return of any civil money penalties.

Subsection (h) would require the Secretary to issue regulations to implement the new authority.

Subsection (i) would provide for the Secretary to deposit the civil money penalties collected under this proposal into the miscellaneous receipts of the Treasury.

Section 108(b) would provide that the new authority would only cover violations of the Act that occur after the effective date of the amendment. It is, however, intended that this legislation be applicable to existing mortgagors as well as those who enter the program in the future.

**AUTHORITY FOR THE SECRETARY TO IMPOSE
CIVIL MONEY PENALTIES ON SECTION 202 MORTGAGORS**

Section 109(a) would amend the Housing Act of 1959 by adding a new section 202a to authorize HUD to impose civil money penalties against mortgagors of property that (1) includes five or more living units and (2) has a mortgage or held pursuant to the Housing Act of 1959. The proposal would authorize the imposition of civil money penalties for certain violations of (A) an agreement entered into as a condition of a transfer of physical assets, a flexible subsidy loan, a capital improvement loan, a modification of the mortgage terms, or a work-out agreement; or (B) the regulatory agreement executed by the mortgagor. The penalty for violation of the agreement described in (A) above could not exceed the amount of the loss the Secretary would experience at a foreclosure sale, or a sale after foreclosure. The penalty for violation of the regulatory agreement would be capped at \$25,000 for each of the specified violations.

The violations for which civil money penalties may be imposed under this section were selected from among the numerous violations which the Department may currently sanction. The Department considers the violations that would be subject to a civil money penalty under this section to be sufficiently egregious to warrant the imposition of a civil money penalty in appropriate circumstances.

While the majority of mortgagors comply with their commitments, the limited sanctions presently available to the Secretary (such as declaring the mortgage in technical default for violation of the regulatory agreement, stopping subsidy payments, or foreclosing on the mortgage) have not been preventing a minority of recalcitrant mortgagors from disregarding their contractual obligations. These sanctions have a more adverse effect on the Department and the tenants than on the mortgagor. The results of the Department's declaration that a mortgage is in default are that the Department discontinues subsidy payments and the Department forecloses on the property at a loss. Due to these events, the project deteriorates physically and financially, with the consequent reduction in services to tenants. To avoid this, it is imperative that the Secretary have the ability to impose sanctions which are commensurate with the harm done by a recalcitrant mortgagor and which would deter mortgagors from disregarding their contractual obligations.

This amendment is similar to other civil money penalty proposals in this bill.

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Need for the Legislation

Civil money penalties have proven to be an effective enforcement tool in Federal programs. Authority to impose civil money penalties for the violations involved here would provide an added incentive for mortgagors to comply with their agreements.

HUD lacks sufficient tools to assure that participants in its programs comply with program requirements. The applicable criminal penalties are often insufficient to ensure enforcement since problems of proof make criminal prosecution difficult. Authorizing the Secretary to impose civil money penalties for violations of specific program requirements will permit HUD more effectively to deter fraud and other violations under HUD programs. The possibility of civil money penalties should also help expedite execution of settlement agreements.

Gaps in existing legislation, primarily the Program Fraud Civil Remedies Act (PFCRA) and the False Claims Act, necessitate this amendment. No penalty can be secured under the PFCRA unless there is a false statement, in the form of a certification, or a false claim. The False Claims Act also requires a false claim. In many of HUD's mortgagor cases, however, certified false statements and false claims have not been involved.

Section-by-Section Analysis

Subsection (a) of proposed section 202a¹ would make clear that the civil money penalty would be in addition to other available civil remedies or any available criminal penalties, and may be imposed whether or not other administrative sanctions are imposed.

Subsection (b)(1) would give the Secretary discretionary authority to impose a civil money penalty on any mortgagor of property that (A) has five or more living units and (B) has a mortgage held pursuant to section 202 of the Housing Act of 1959 where the mortgagor has (i) a written agreement, executed as a condition of a transfer of physical assets, a flexible subsidy loan, a capital improvement loan, a modification of the mortgage terms, or a work-out agreement, to use non-project income (ii) to make cash contributions for payments due under the note and mortgage, for payments to the reserve for replacements, to restore the project to good physical condition, or to pay other project liabilities, for failure to comply with any of these

¹All future references to subsections refer to subsections of proposed section 202a of the Housing Act of 1959, except for the reference in the last paragraph, which refers to subsection (b) of this proposed section of this bill.

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commitments. (The reference to "Secretary" includes another department official.)

In most instances, where one of these agreements is executed, the Secretary agrees to provide additional subsidy resources or to forego mortgage payments for a period of time, and, in consideration of the Secretary's agreement, the mortgagor agrees to provide additional cash contributions to the project income stream to restore the project to acceptable financial and physical condition. If, after the Secretary has provided the additional resources, the owner fails to make the agreed upon cash contribution, the project will not be restored and the Department's section 202 loan fund will be further jeopardized.

Subsection (b)(2) would limit the amount of the civil money penalty for a violation of subsection (b)(1) to the amount of the loss the Secretary would experience at a foreclosure sale, or a sale after foreclosure.

Subsection (c)(1) would give the Secretary discretionary authority to impose a civil money penalty against any mortgagor of property that (A) has five or more living units and (B) has a mortgage held pursuant to section 202 of the Housing Act of 1959 for violations of the regulatory agreement executed by the mortgagor, as specified in subparagraphs (A)-(M).

Paragraph (1)(A) would provide for the imposition of a civil money penalty for the conveyance, transfer, or encumbrance of any of the mortgaged property, or for permitting such action without the prior written approval of the Secretary.

Paragraph (1)(B) would provide for the imposition of a civil money penalty for the assignment, transfer, disposition, or encumbrance of any personal property of the project, including rents, or paying out any funds, except for reasonable operating expenses and necessary repairs, without the prior written approval of the Secretary.

Paragraph (1)(C) would provide for the imposition of a civil money penalty for the conveyance, assignment, or transfer of any beneficial interest in any trust holding title to the property, or the interest of any general partner in a partnership owning the property, or any right to manage or receive the rents and profits from the mortgaged property, without the prior written approval of the Secretary.

Paragraph (1)(D) would provide for the imposition of a civil money penalty for remodeling, adding to, reconstructing, or demolishing any part of the mortgaged property or subtracting from any real or personal property of the project, without the prior written approval of the Secretary.

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Paragraph (1)(E) would provide for the imposition of a civil money penalty where the mortgagor, as a condition of the occupancy or leasing of any unit in the project, requires any consideration or deposit other than the prepayment of the first month's rent, plus a security deposit in an amount not in excess of one month's rent, to guarantee the performance of the covenants of the lease. This paragraph is designed to protect low- and moderate-income tenants and assure equal access for all applicants.

Paragraph (1)(F) would provide for the imposition of a civil money penalty for the failure to keep any funds collected as security deposits separate and apart from all other funds of the project in a trust account, the amount of which at all times equals or exceeds the aggregate of all outstanding obligations under that account. This paragraph is designed to prevent use of the tenants' security deposits for project costs and, thus, assure the availability of these moneys when the tenants vacate the premises, provided that the premises are returned to the mortgagor in good condition.

Paragraph (1)(G) would provide for the imposition of a civil money penalty for paying over \$500 for services, supplies, or materials when such payment substantially exceeds the amount ordinarily paid for such services, supplies, or materials in the area where the services are rendered or the supplies or materials furnished. While the majority of mortgagors are cost conscious, a minority do not adequately contain costs for reasons such as the lack of professional ability to do so; the receipt of kickbacks from the provider of the services, supplies, or materials; or an identity of interest with the firm supplying the services, supplies, or materials. This has an adverse impact on tenants whose rents are set at a level to pay for these costs. It can also have an adverse impact on the Department where it provides rent subsidies, or where the overpayment contributes to an insurance claim.

Paragraph (1)(H) would provide for the imposition of a civil money penalty for failure to maintain at any time the mortgaged property, equipment, buildings, plans, offices, apparatus, devices, books, contracts, records, documents, and other related papers (including the failure to keep copies of all written contracts or other instruments which affect the mortgaged property) in reasonable condition for proper audit and for examination and inspection at any reasonable time by the Secretary or the Secretary's duly authorized agents. If the Secretary is to monitor and enforce mortgagor compliance with program requirements, it is imperative that these requirements be met.

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Paragraph (1)(I) would provide for the imposition of a civil money penalty for failure to maintain the books and accounts of the operations of the mortgaged property and of the project in accordance with requirements prescribed by the Secretary. If the Secretary cannot impose sanctions to enforce compliance on the minority of recalcitrant mortgagors who fail to comply with this requirement, program enforcement is jeopardized since the project's cash flow is the cornerstone for maintaining the project in a good fiscal and physical condition.

Paragraph (1)(J) would provide for the imposition of a civil money penalty for failure to furnish the Secretary, within 60 days following the end of each fiscal year, with a complete annual financial report based upon an examination of the books and records of the mortgagor, prepared and certified to by an independent public accountant or a certified public accountant and certified to by an officer of the mortgagor, unless the Secretary has approved an extension of the 60-day period in writing.

Paragraph (1)(K) would provide for the imposition of a civil money penalty when, at the request of the Secretary, the agents of the Secretary, the employees of the Secretary, or the attorneys of the Secretary, the mortgagor fails to furnish monthly occupancy reports or fails to provide specific answers to questions upon which information is sought relative to income, assets, liabilities, contracts, the operation and condition of the property, or the status of the insured mortgage.

Mortgagors of financially and physically solvent projects are not required to provide the Department with monthly accountings of cash income and outlays. When the Department becomes aware, however, that a mortgagor is having financial problems with regard to a particular project, it will require the mortgagor to provide monthly accounts of income and disbursements. This is necessary to assure the proper future maintenance of the project for the benefit of the tenants and to protect the Department from claims on the insurance funds.

Paragraph (1)(L) would provide for the imposition of a civil money penalty for failure to make promptly all payments due under the note and mortgage, including tax and insurance escrow payments, and payments to the reserve for replacements when there is adequate project income available to make such payments. This provision is designed to avoid having the mortgage go into default when there is adequate project income available for the required payments.

Paragraph (1)(M) would provide for the imposition of a civil money penalty for amendment of the mortgagor's articles of incorporation or by-laws, other than as permitted under the terms of the articles of incorporation approved by the Secretary,

without the prior written approval of the Secretary. This paragraph is designed to assure the maintenance of the nonprofit status of the mortgagor and the regulatory controls imposed by HUD.

Subsection (c)(2) would cap the amount of the civil money penalty for a violation of subparagraphs (A)-(M) at \$25,000 for a violation of any of those subparagraphs. The monetary penalties that would be provided under subsection (c)(2) are similar to civil money penalties that are provided in many other Federal statutes which authorize the administrative imposition of such penalties.

Subsection (d)(1) would require that the Secretary establish standards and procedures governing HUD's imposition of civil money penalties under subsections (b) and (c). In accordance with subparagraph (A), the Secretary or other department official (such as the Assistant Secretary for Housing) could make the determination to impose the penalty. In accordance with subparagraph (B), the standards and procedures would provide that the civil money penalty could not be imposed before the mortgagor had an opportunity for a hearing on the record by an Administrative Law Judge. Subparagraph (C) would authorize HUD to establish standards and procedures providing for review of any determination or order, or interlocutory ruling, arising from a hearing. If a hearing is not requested within 15 days of receipt of the notice of opportunity for hearing, the imposition of the civil money penalty would be a final and unappealable determination. If the Secretary reviews the determination or order of the Administrative Law Judge, the Secretary may affirm, modify, or reverse that determination or order. If the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order would be the final determination or order of the Secretary.

In implementing the proposed civil money penalty authority, the Department contemplates using, to the maximum extent possible, the existing review procedures in 24 CFR Part 26 (Proceedings Before a Hearing Officer). Thus, the new authority would be coupled with a well-known, existing procedure.

Subsection (d)(2) would set forth factors to be considered in determining the amount of the civil money penalty. These would consist of the gravity of the offense, any history of prior offenses (including those before enactment of this proposal), the ability of the borrower to pay the penalty, injury to the public, benefits received, deterrence of future violations, and such other factors as the Secretary determines in regulations to be appropriate.

Subsection (e) would give mortgagors the right to judicial review in the U.S. Court of Appeals. The court also would have

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jurisdiction to consider any ancillary issues, such as administrative sanctions, covered by the notice of determination to impose a penalty under subsection (d). Subsection (e) would also make it clear that the reviewing court has the authority to order payment of the civil money penalty. This would avoid the possibility of the court's upholding a determination or order imposing a civil money penalty without ordering payment, which could necessitate additional litigation to secure payment. As is the existing practice with respect to other civil monetary penalties, the findings and determinations of the Secretary in imposing civil money penalties would not be subject to trial de novo by the reviewing court.

Under subsection (f), the Department could request the Attorney General to institute an action in an appropriate U.S. district court against a person that fails to pay a civil money penalty after it has become a final and unappealable order. The action would seek a money judgment against the person as well as any other relief that may be available. The money judgment could include attorneys' fees and other expenses of the United States in bringing the action. The validity and appropriateness of the final order imposing the civil money penalty would not be subject to the review.

Subsection (g) would give the Secretary discretion to compromise, modify, or remit any civil money penalty before or after it has been imposed. Since it is the goal of this proposal to achieve compliance with the requirements of programs administered by the Department, subsection (g) would permit the Secretary to enter into settlements which would provide for such compliance, including compromise, modification, or return of any civil money penalties.

Subsection (h) would require the Secretary to issue regulations to implement the new authority.

Subsection (i) would provide for the Secretary to deposit the civil money penalties collected under this proposal into miscellaneous receipts of the Treasury.

Section 109(b) would provide that the new authority would only cover violations of the Act that occur after the effective date of the amendment. It is, however, intended that this legislation be applicable to existing mortgagors as well as those who enter the program in the future.

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**AUTHORITY FOR THE SECRETARY TO IMPOSE CIVIL MONEY
PENALTIES ON GNMA ISSUERS**

Section 110 would amend the National Housing Act by adding a new section 317, which would authorize the Secretary to impose civil money penalties on an issuer of GNMA mortgage-backed securities or a GNMA custodian for the specific violations of GNMA program requirements, as applicable, including:

- (1) failure to make timely payments of principal and interest (P&I) to security holders;
- (2) failure to properly segregate cash flow from mortgages;
- (3) improper use of escrows;
- (4) transfer of pool servicing to an issuer not approved by GNMA;
- (5) failure to maintain GNMA's standards for minimum net worth;
- (6) failure of an issuer to notify GNMA of a change in business status;
- (7) submission of false information or a false certification to GNMA; and
- (8) hiring an individual or retaining an employee when the issuer or custodian knew, or should have known, that the individual or employee was suspended or debarred from HUD programs.

The penalty under this proposal would be \$5,000 per violation, with a \$1 million cap per violator for any related series of violations occurring during any one-year period. In the case of a continuing violation, each day would constitute a separate violation. There would be an opportunity for a hearing before an Administrative Law Judge and judicial review of the decision by the Secretary.

HUD lacks sufficient tools to assure that participants in its programs comply with program requirements. The applicable criminal penalties are often insufficient to ensure enforcement since problems of proof make criminal prosecution difficult. Authorizing the Secretary to impose civil money penalties for violations of specific program requirements will permit HUD more effectively to deter fraud and other violations under HUD programs, thus strengthening the sanctioning process. The possibility of civil money penalties also should help expedite execution of settlement agreements.

This amendment is similar to other civil money penalty proposals in the bill.

Section-by-Section Explanation

Subsection (a)(1)⁴ would give the Secretary discretionary authority to impose a civil money penalty against a GNMA issuer or custodian that violates the requirements set forth in subsection (b). (The reference to "Secretary" includes another department official.) The civil money penalty would be in addition to other available civil remedies or any available criminal penalties, and may be imposed whether or not other administrative sanctions are imposed.

Subsection (a)(2) would limit the amount of the civil money penalty to \$5,000 for each violation, except that the maximum penalty for all violations committed by a GNMA issuer or custodian during any one-year period could not exceed \$1 million. In the case of a continuing violation, each day would constitute a separate violation. These monetary standards are similar to many other civil money penalty provisions.

Subsections (b)(1)(A)-(J) would list the violations which may warrant the imposition of civil money penalties. The Department considers these violations to be sufficiently egregious to warrant the imposition of civil money penalties in appropriate circumstances. Subparagraph (b)(1)(K) covers violations of other statutory and administrative requirements.

Subsection (b)(1)(A) would provide for the imposition of a civil money penalty when a GNMA issuer fails to make a timely pass-through of principal and interest (P&I) payments from pooled mortgages to holders of GNMA securities. Timely receipt of P&I by investors is the cornerstone of the GNMA mortgage-backed securities program, and failure by an issuer to comply with this GNMA program requirement reduces investor confidence and increases expenditures by GNMA under its guaranty of timely payment to investors.

Subsection (b)(1)(B) would provide for the imposition of a civil money penalty when a GNMA issuer (as a mortgage servicer) fails to segregate all funds received from a mortgagor, whether P&I funds or escrow funds, or fails to deposit these funds in special custodial accounts with a depository institution whose

⁴ All references to subsections refer to subsections of proposed new section 317 of the National Housing Act, except for the reference in the last paragraph, which refers to subsection (b) of this proposed section of this bill.

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accounts are insured by the National Credit Union Administration or by the Federal Deposit Insurance Corporation through the Bank Insurance Fund for banks and through the Savings Association Insurance Fund for savings associations. A failure to segregate escrow funds would make accounting for these amounts difficult and could encourage the improper diversion of these funds or other illegal activity. Diversion or failure to place these funds in insured accounts could result in increased GNMA expenditures (for P&I pass-through payments to investors) or increased mortgagor expenditures and/or default (for payment of escrow items such as taxes and insurance).

Subsection (b)(1)(C) would provide for the imposition of a civil money penalty when a GNMA issuer or custodian uses escrow funds for any purpose other than that for which they were received.

Subsection (b)(1)(D) would provide for the imposition of a civil money penalty when a GNMA issuer transfers servicing of a pool of mortgages to a servicer that has not been approved by GNMA, unless the transfer is expressly permitted by statute, regulation, or contract approved by the Secretary. Title III of the National Housing Act, known as the "Charter Act," contemplates that GNMA will provide a guarantee to security holders only with regard to a pool of mortgages serviced by an issuer that meets the requirements of the Charter Act. GNMA funds are at risk when a pool of mortgages is transferred to an issuer that does not meet these requirements.

Subsection (b)(1)(E) would provide for the imposition of a civil money penalty when a GNMA issuer fails to maintain a minimum net worth. GNMA funds are at risk if an issuer has insufficient financial resources to make timely payment on GNMA-guaranteed securities from its own funds when payments on pooled mortgages are delinquent.

Subsection (b)(1)(F) would provide for the imposition of a civil money penalty if an issuer fails to notify GNMA of a substantial change in its business status. For example, GNMA funds could be at risk if ownership of an issuer (and responsibility for servicing of pooled mortgages) changes without approval from GNMA.

Subsection (b)(1)(G) would provide for the imposition of a civil money penalty when an issuer or a custodian knew, or should have known, that information submitted to the Secretary was false. Issuers must provide accurate information if GNMA is to avoid costly claims on its guaranty of mortgage-backed securities. Under this provision, an issuer or a custodian would be subject to a civil money penalty if any of its employees knew, or should have known, that information submitted to GNMA was false.

Subsection (b)(1)(H) would permit the Secretary to impose a civil money penalty when an issuer or custodian hires an officer, director, principal, or employee whose duties will involve GNMA programs, directly or indirectly, when the issuer or custodian knew, or should have known, that the person was under suspension or debarment by the Secretary. Penalties also could be imposed when an issuer or custodian employs an officer, director, principal, or employee who continues to be involved in GNMA programs, directly or indirectly, when the issuer or custodian knew, or should have known, that the person was under suspension or debarment by the Secretary.

Subsection (b)(1)(I) would permit the Secretary to impose a civil money penalty on an issuer or custodian that submits a false certification to GNMA. Costly claims against GNMA could result from false certifications. This subsection also would permit the Secretary to impose a civil money penalty on an issuer that knowingly submits a false certification by another person or entity.

Subsection (b)(1)(J) would permit the Secretary to impose a civil money penalty on an issuer that fails to comply with an agreement, certification, or condition of approval set forth on, or applicable to, the application for approval as an issuer by GNMA. Approval by GNMA is conditioned upon commitments made by the issuer in its issuer application as well in the process of forming a pool of mortgages backing GNMA-guaranteed securities. For example, an issuer agrees to permit an examination of its records and accounts by GNMA. Failure of an issuer to comply with this commitment could put GNMA funds at risk.

Subsection (b)(1)(K) would permit the Secretary to impose a civil money penalty for the violation of any provisions of the Charter Act or any implementing regulation, handbook, or GNMA participant letter that is issued under the Charter Act. Since legislation cannot provide for every conceivable violation, this subsection would give the Secretary the flexibility to impose civil money penalties for violations of any other requirements in the Charter Act.

Subsection (b)(2) would require the Secretary to inform the Attorney General of the United States before taking action to impose a civil money penalty for a violation described in subsection (b)(1)(G) or (b)(1)(I).

Subsection (c)(1) would require that the Secretary establish standards and procedures governing HUD's imposition of civil money penalties under subsection (a). Under subsection (c)(1)(A), the standards would provide for the Secretary to make the determination to impose the penalty. Under subsection (c)(1)(B), the standards and procedures would provide

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that the civil money penalty could not be imposed before the issuer or the custodian had an opportunity for a hearing on the record before an Administrative Law Judge. If a hearing is not requested within 15 days of receipt of a notice of opportunity for hearing, the imposition of the civil money penalty would constitute a final and unappealable determination. Subsection (c)(1)(C) would authorize HUD to establish standards and procedures providing for review of any determination or order, or interlocutory ruling, arising from a hearing.

Subsection (c)(1)(C) would also provide that if the Secretary reviews the determination or order of the Administrative Law Judge, the Secretary may affirm, modify, or reverse that determination or order. If the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order would be the final determination or order of the Secretary.

In implementing the proposed civil money penalty authority, the Department contemplates using, to the maximum extent possible, the existing review procedures in 24 CFR Part 26 (Proceedings Before a Hearing Officer). Thus, the new authority would be coupled with a well-known, existing procedure.

Subsection (c)(2) would set forth the factors to be considered in determining the amount of the civil money penalty. These factors would include the gravity of the offense, any history of prior offenses (including those before enactment of this amendment), the ability of the issuer or the custodian to pay the penalty, injury to the public, benefits received, deterrence of future violations, and such other factors as the Secretary determines through regulations.

Subsection (d) would give issuers and custodians the right to judicial review in a U.S. court of appeals. The court also would have jurisdiction to consider any ancillary issues covered by the notice of determination to impose a penalty under subsection (c). Subsection (d) would clarify that the reviewing court has the authority to order payment of the civil money penalty. This clarification would avoid the possibility of the court's upholding a determination or order imposing a civil money penalty without ordering payment, as is the practice with other civil monetary penalties, which could necessitate additional litigation to secure payment. The findings and determinations of the Secretary in imposing money penalties would not be subject to trial *de novo* by the reviewing court.

Under subsection (e), the Department could request the Attorney General to institute an action in an appropriate U.S. district court against an issuer or a custodian that fails to pay a civil money penalty after the penalty becomes a final and unappealable order. The action would seek a money judgment

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against the issuer or the custodian, as well as any other relief that may be available. The money judgment could include attorneys' fees and other expenses of the United States in bringing the action. The validity and appropriateness of the final order imposing the civil money penalty would not be subject to review.

Subsection (f) would give the Secretary discretion to compromise, modify, or remit any civil money penalty before or after it has been imposed. The goal of this legislative proposal is to achieve compliance with the requirements of programs administered by the Department; consequently, subsection (f) would permit the Secretary to enter into settlements which would provide for such compliance, including compromise, modification, or return of any civil money penalties.

Subsection (g) would require the Secretary to issue regulations to implement the new authority.

Subsection (h) would provide for the Secretary to deposit all civil money penalties collected under this legislative amendment into miscellaneous receipts of the Treasury.

Section 110(b) would provide that the new authority would only cover issuer violations that occur after the effective date of the amendment. In the case of a continuing violation (as determined by the Secretary), the new authority would apply to any portion of the violation occurring on or after that effective date.

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**AUTHORITY FOR THE SECRETARY TO IMPOSE CIVIL MONEY
PENALTIES FOR VIOLATIONS OF THE INTERSTATE LAND
SALES FULL DISCLOSURE ACT**

Section 111 would amend section 1423 of the Interstate Land Sales Full Disclosure Act to authorize HUD to impose civil money penalties against land developers for violations of the Act which relate to: the failure to register non-exempt subdivisions; the failure to provide full and accurate disclosure to consumers; and the use of deception, misrepresentation, or fraud in the promotion and sale of their properties. The penalties under this proposal would be \$1,000 per violation, up to \$1 million a year per violator for any related series of violations, after opportunity for a hearing. In the case of a continuing violation, each day would constitute a separate violation.

This amendment is similar to other civil money penalty proposals in the bill.

Civil money penalties have proven to be an effective enforcement tool in Federal programs. Authority to impose civil money penalties for the violations involved here would provide an added incentive for developers to comply with the Interstate Land Sales Act's requirements, thereby resulting in more accurate and complete disclosure to the public. The provision that, in the case of a continuing violation, each day will constitute a separate violation will also increase the incentive for developers to comply with the Act. One of the common violations of the Act is the failure to register non-exempt subdivisions with HUD, which is a continuing violation.

HUD lacks sufficient tools to assure that participants in its programs comply with program requirements. The applicable criminal penalties are often insufficient to ensure enforcement since problems of proof make criminal prosecution difficult. Authorizing the Secretary to impose civil money penalties for violations of specific program requirements will permit HUD more effectively to deter fraud and other violations under HUD programs. The possibility of civil money penalties should also help expedite execution of settlement agreements.

Currently, the most serious civil sanction HUD can impose administratively for violations of the Interstate Land Sales Full Disclosure Act is the relatively mild one of requiring that developers offer refunds to affected purchasers. In order to secure a more severe civil penalty, the Department must file suit in Federal court seeking an injunction and ancillary relief. Because court action is lengthy and labor-intensive, HUD cannot file many suits, and even where it has filed and prevailed, sanctions have not been imposed quickly. Although the Act also provides for criminal suits, this is a limited enforcement tool since the violations must be willful. Accordingly, few criminal

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prosecutions have been brought. Where such actions have been brought and decisions rendered for the government, penalties have not been imposed quickly. As a result, a significant number of developers have chosen to take the risk of violating the Act. The potential imposition of a monetary fine, in addition to the existing penalties, would curtail, if not extinguish, this attitude.

The penalty provided by this proposal would be \$1,000 per violation although it would be \$5,000 under the proposal authorizing penalties against FHA mortgagees and lenders. This proposal would provide for a lower penalty per violation because (1) the higher penalty would be unduly burdensome to companies in the land sales industry; and (2) there is apt to be a greater number of violations of the Interstate Land Sales Full Disclosure Act than of FHA program requirements, and, accordingly, a lower penalty per violation can serve as a deterrent.

Subsection (a)(1)⁵ would give the Secretary discretionary authority to impose a civil money penalty against any person who violates any of the provisions of the Interstate Land Sales Full Disclosure Act, or any rule, regulation, or order issued under it. It would make clear that the money penalty would be in addition to other available civil remedies or any available criminal penalties, and may be imposed whether or not other administrative sanctions are imposed.

Subsection (a)(2) would limit the amount of the civil money penalty to \$1,000 for each violation, except that the maximum penalty for all violations committed by a developer during any one-year period could not exceed \$1 million. In the case of a continuing violation, each day would constitute a separate violation. These monetary standards are similar to many other civil money penalty provisions.

Subsection (b)(1) would require that the Secretary establish standards and procedures governing HUD's imposition of civil money penalties under subsection (a). (The reference to "Secretary" includes another department official.) In accordance with subsection (b)(1)(A), the standards and procedures would provide that the civil money penalty could not be imposed by the Secretary before the developer had an opportunity for a hearing on the record by an Administrative Law Judge. If no hearing is requested within 15 days of receipt of the notice of opportunity for hearing, the imposition of the penalty would constitute a final and unappealable determination. Subsection (b)(1)(B) would

⁵ All references to subsections refer to subsections of proposed revised section 1423 of the Interstate Land Sales Full Disclosure Act, except for the reference in the last paragraph, which refers to subsection (b) of this section of this bill.

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authorize HUD to establish standards and procedures providing for review of any determination or order, or interlocutory ruling, arising from a hearing. If the Secretary reviews the determination or order of the Administrative Law Judge, the Secretary may affirm, modify, or reverse that determination or order. If the Secretary does not review the determination or order of the Administrative Law Judge, the determination or order would be the final determination or order of the Secretary.

In implementing the proposed civil money penalty authority, the Department contemplates using, to the maximum extent possible, the existing review procedures in 24 CFR Part 26 (Proceedings Before a Hearing Officer). Thus, the new authority would be coupled with a well-known, existing procedure.

Subsection (b)(2) would set forth factors to be considered in determining the amount of the civil money penalty. These would consist of the gravity of the offense, any history of prior offenses (including those before enactment of this proposal), the ability of the developer to pay the penalty, injury to the public, benefits received, deterrence of future violations, and such other factors as the Secretary determines in regulations to be appropriate.

Subsection (c) would provide for judicial review in a United States court of appeals, as provided currently in section 1411 of the Act. Subsection (c) would also make it clear that the reviewing court has the authority to order payment of the civil money penalty.

Under subsection (d), the Department could request the Attorney General to institute an action in an appropriate U.S. district court against a person that fails to pay a civil money penalty after it has become a final and unappealable order. The action would seek a money judgment against the person as well as any other relief that may be available. The money judgment could include attorneys' fees and other expenses of the United States in bringing the action. The validity and appropriateness of the final order imposing the civil money penalty would not be subject to the review.

Subsection (e) would give the Secretary discretion to compromise, modify, or remit any civil money penalty before or after it has been imposed. Since it is the goal of this proposal to achieve compliance with the requirements of programs administered by the Department, subsection (e) would permit the Secretary to enter into settlements which would provide for such compliance, including compromise, modification, or return of any civil money penalties.

Subsection (f) would require the Secretary to issue regulations to implement the new authority.

Subsection (g) would provide for the Secretary to deposit the civil money penalties collected under this proposal into miscellaneous receipts of the Treasury.

Section 111(b) would provide that the new authority would only cover violations of the Act that occur after the effective date of the amendment. In the case of a continuing violation (as determined by HUD), the new authority would apply to any portion of the violation occurring on or after that effective date.

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CONSULTANT REFORMS

Section 112 would establish a strict requirement that consultants, lobbyists, and lawyers who attempt to influence departmental decisions for clients attempting to obtain assistance from HUD or that are involved in a management action (including sanctions), must register with the Department. In addition, all those applying for assistance or involved in a management action would be required to disclose any fees paid to consultants, lobbyists, and lawyers to influence the Department's decision. The Secretary would have the authority to deduct any such fees from the amount of assistance, reduce the amount of insurance for which the applicant otherwise would have been eligible by the amount of the fees, or take the fees into account when taking the management action. The Secretary also would have the authority to impose civil money penalties of up to \$10,000 for each failure to register or to provide information with respect to fees.

Persons who spend or receive less than \$5,000 in any calendar quarter and less than \$10,000 in any Federal fiscal year to influence a departmental decision would be exempt from the reporting and registration requirements of this section. This would allow, for example, PHA consultants to provide necessary technical and professional assistance to PHAs without subjecting either the PHAs or consultants to the requirements of this section.

Many of HUD's worst problems first came to light in the Inspector General's reports to Congress. Among the issues addressed in these reports were allegations that housing grants had been awarded to certain developers who paid huge fees to politically connected consultants and lobbyists who did little more than open doors and place phone calls. In the past, politically connected consultants have received as much as \$1,500 per unit to arrange funding awards in advance of public notice. This section would help assure that influence peddlers who earn substantial sums of money for making a few phone calls would be put out of business. If such activities had been subject to the requirements of this section, they never would have happened.

This section would require each person who makes an expenditure (above the threshold) to influence a departmental decision with respect to any assistance within the jurisdiction of the Department or any management action with respect to such assistance to file annual reports with the Secretary. The term "assistance within the jurisdiction of the Department" would include any contract, grant, loan, cooperative agreement, or other form of assistance, including the insurance or guarantee of a loan, mortgage, or pool of mortgages. The term "management action" would include any action involving any assistance within the jurisdiction of the Department that has been, or is planned

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to be, taken, or is under consideration, including any administrative sanction, recovery or conditioning of assistance, abatement of rents in whole or in part, determination of default, or any other measure affecting any person. It also would require each person who receives payment to influence such departmental decisions to register with the Secretary and to file annual reports for as long as the activity continues. Both types of reports would be published in the Federal Register.

The reports would contain detailed information with respect to expenditures made or payments received to influence departmental decisions, including the persons, amounts, dates, and purposes involved. However, the reports would exclude payment of reasonable compensation made to regularly employed officers and employees of the person who requests or receives assistance within the jurisdiction of the Department, or who is involved in any management action with respect to such assistance.

This section also would authorize the Secretary to impose civil money penalties of up to \$10,000 for each violation for failure to file the reports required under this section. (The reference to "Secretary" would include another department official or an administrative entity.) The authority to impose this penalty would be in addition to any other available civil remedy or any available criminal penalty, and could be imposed whether or not the Secretary imposes other administrative sanctions. The person against whom the Secretary assesses a penalty would have an opportunity for a hearing by an Administrative Law Judge. After exhausting all administrative remedies, the person could file an appeal with the appropriate court of appeals of the United States. HUD would deposit civil money penalties collected under this section into miscellaneous receipts of the Treasury.

The section would take effect on the date specified in regulations implementing this section that are issued by the Secretary after notice and public comment. The regulations would establish standards that include determinations of what types of activities constitute influence with respect to departmental assistance decisions and management actions.

The Department notes that this section would overlap with the consultant reform provision (Byrd Amendment) in the Department of Interior appropriations Act (P.L. 101-121), which was signed by the President on October 23, 1989. However, in light of the problems at HUD with respect to consultants that have recently been uncovered, the Department believes that it needs the unique features of this consultant reform provision to address these problems. This provision differs from the Byrd Amendment in several respects, including: (1) the requirement that consultants register with HUD or be subject to a penalty;

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(2) the extension of coverage to management actions, including sanctions; and (3) the authorization of the Secretary to deduct consultant fees from assistance. The Department will work with Congress to eliminate the overlap between these two provisions.

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TITLE II -- MANAGEMENT REFORM

APPOINTMENT OF CHIEF FINANCIAL OFFICER AND
FHA COMPTROLLER

Section 201 would amend section 4 of the Department of Housing and Urban Development Act to require the Secretary to appoint a Chief Financial Officer (CFO) and an FHA Comptroller. The CFO would be selected on the basis of demonstrated ability in financial management and financial systems development and operations, and would serve as the principal advisor to the Secretary on financial management. The CFO would, among other things, be responsible for (1) developing and maintaining a financial management system for the Department, (2) supervising and coordinating all financial management activities and operations of the Department, and (3) assisting in the financial execution of HUD's budget. The Chief Financial Officer would report to the Secretary through the Under Secretary.

The FHA Comptroller would be designated by the Secretary and report directly to the Assistant Secretary for Housing/FHA Commissioner. The Comptroller would conduct activities within the overall financial management systems developed and operated by the CFO. Responsibilities of the FHA Comptroller would include preparation of comprehensive FHA internal financial statements, maintaining the FHA general ledger and subsidy ledgers, and other activities related to the financial operations of FHA.

The appointment of these two officials would greatly assist the Department in resolving current financial problems due to past financial mismanagement and fraud, and would ensure against future financial mismanagement and fraud. In recent testimony on FHA performance, a representative of the General Accounting Office stated that the appointment of a chief financial officer within HUD and a corresponding comptroller in FHA would be an important part of the solution to HUD/FHA financial problems.

For example, inadequate attention paid by HUD officials and employees to the reconciliation of accounts, management reports, and cash tracking contributed to the recent cases of embezzlement of FHA funds by closing agents. Essentially, no one person at HUD (below the Secretarial level) was responsible for making sure that the different housing program offices and housing computer systems were working together to prevent fraud. The Chief Financial Officer and FHA Comptroller could prevent a reoccurrence of these types of theft since they would be responsible for ensuring that cash management systems are tightly controlled.

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Moreover, section 301 of this bill would require FHA to publish annual audited financial statements, prepared by an independent accounting firm. The FHA Comptroller would be responsible for ensuring that all accounting systems are well-managed and capable of being fully audited every year. Results would be consolidated with the HUD general ledger under the auspices of the Chief Financial Officer and then transmitted to the Congress and published each year.

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PROGRAM EVALUATION AND MONITORING

Section 202 would authorize the Secretary to use up to 0.5% of the amounts appropriated for the programs noted below for evaluation and monitoring of these programs (including the entire public housing and section 202 programs). The specific amount that could be drawn from each program would be set forth in an appropriation Act. In addition to specifying the amount, the appropriation Act would also specify the account to which the specified amounts would be transferred, i.e., Salaries and Expenses, Research and Technology, or possibly others. The programs affected would be these:

Public and Indian housing development and modernization
 Section 202 rental handicapped assistance
 Counseling
 Fair Housing Assistance
 CDBG and Urban Homesteading
 Section 8 rental assistance
 Flexible subsidy
 Congregate housing
 Child care demonstration
 Fair Housing Initiatives
 McKinney Act homeless assistance, and
 Rental Rehabilitation.

HUD spends between \$17 and \$18 billion per year in grants and assistance, but less than \$25 million for evaluation, monitoring, and related research to detect flaws in program design and improve program operations. Funding for HUD's Office of Policy Development and Research has dropped from \$50 million in 1980 to \$17 million in 1989. Of this, less than \$6 million is available for new activities; the rest is committed to continue the American Housing Survey and other Census-conducted surveys, as required by law. Accordingly, essential program evaluations and monitoring activities have been postponed.

The section 8 rental assistance program illustrates the need for better evaluation information. The Department lacks complete records for about the 2.4 million households that it assists at a cost of approximately \$10 billion per year, as well as other information needed to evaluate where program improvements are needed. Increased expenditures for evaluation and monitoring will be more than offset by averting unnecessary payments, waste, and fraud in connection with the section 8 and other programs of the Department. The kinds of evaluation activities the Department would consider undertaking under this proposal include:

- Homeownership and Affordable Housing. Evaluations of the effectiveness of various housing assistance

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programs in reaching the appropriate population, in improving the housing and general living conditions of recipients, and in increasing economic opportunities for recipients. These evaluations will assess how different assistance strategies work for different populations and in different economic conditions. Evaluations of techniques to prevent or cure default problems in multifamily projects.

- Homelessness. Evaluations of the HUD McKinney Act programs to determine if funds are reaching the people who need help and are being used effectively, as well as evaluations of the impact of homeless assistance on recipients, including its effectiveness in keeping formerly homeless people from becoming homeless again.
- Drug-Free Public Housing. Evaluations of the effectiveness of strategies to reduce the vulnerability of particular housing environments to drugs and evaluations of the impact of successful strategies on tenant living conditions and tenant economic status.
- Resident Management and Homesteading. Evaluations of the effectiveness of resident management corporations (RMCs) in improving tenant living conditions; and evaluations of urban homesteading programs.
- Economic Development and Enterprise Zones. New evaluations of the entitlement and State CDBG programs and the development of baseline data for determining the impact of enterprise zones.
- Fair Housing. Evaluations to determine the effectiveness of HUD's implementation of the new fair housing law, and of activities funded by the Fair Housing Initiatives program, in combatting discrimination against minorities and other protected classes.

Only programs for which grant or other assistance funds are appropriated would be subject to the set-aside. The insurance and direct loan programs (other than Housing for the Elderly and Handicapped) do not receive such appropriations, and would not be covered by this proposal. The Research and Technology and Salaries and Expenses accounts, and in some circumstances the FHA Funds themselves, would normally be available to fund activities similar to those contemplated in this proposal. The amount appropriated for the Public Housing Operating Subsidy program also would not be affected, since the amount appropriated for that program is intended to be 100% of the amount necessary to provide for the operation of public housing. The amounts

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available for public housing, however, could be used to evaluate and monitor the entire program.

Finally, to assure that all amounts set aside are used expeditiously, the amount set aside would be centrally controlled and any amounts that remain available for obligation at the end of the fiscal year after the fiscal year for which they were appropriated would be rescinded.

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EXPEDITING HUD RULEMAKING

Section 203 would make a small but significant change in the congressional review procedures that apply to the production of HUD rules. The change is designed to retain the existing machinery for congressional oversight of HUD rules, while avoiding the extended production delays that are an unintended, but sometimes severe, harmful side effect of the present law.

Current Section 7(o)

Section 7(o) of the Department of Housing and Urban Development Act--HUD's legislative review statute--was adopted in 1978 as a means of strengthening congressional oversight of the regulations development process at HUD. The statute has the following principal features:

--Semiannual Agenda of Regulation. HUD is required twice annually to submit to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Banking, Finance and Urban Affairs of the House of Representatives an agenda of all regulations that the Department has under development or review.

--Rules to be published for comment. The Department may not publish for comment in the Federal Register any regulation on the Semiannual Agenda for 15 "congressional session days" after the Agenda's submission. If, within this period, either Banking Committee requests review of particular regulations on the Agenda that are to be published for comment, each requested regulation must be submitted to both Committees for a period of 15 "congressional session days" before it is published.

--Rules published for effect. Any HUD rule published for effect must have its effectiveness delayed for 30 "congressional session days" after its date of publication. If, during that period, either Committee reports out, or is discharged from further consideration of, a joint resolution of disapproval or other legislation intended to modify or invalidate the regulation, the rule's effectiveness must be delayed for an additional 90 calendar days from the date of the Committee's action.

--Calculation of "congressional session days". The 15- and 30-day clocks must begin anew if interrupted by an adjournment of Congress sine die, and the count of "congressional session days" is suspended during any recess of either House of more than three days.

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Deficiencies in the Current Process

Section 7(o) suffers from a major defect. Use of "congressional session days" to calculate the 15- and 30-day waiting periods has seriously impeded the Department's ability to implement its regulatory priorities. The congressional calendar for each year is sprinkled with recesses, including an "August recess" of about a month. The longer the waiting period, the greater the delay in the Department's ability to promptly publish rules that either Committee has selected from the Agenda, or to make any published rule effective.

The delays have been particularly troublesome where Congress adjourns sine die. These adjournments typically occur in October or November and continue until Congress returns the following January. The "dead time" occasioned by adjournments sine die can delay the effectiveness of a published rule for five months or more.

The treatment of HUD rules at the end of the 100th Congress (last year) provides a good example of the excessive delays brought about by the present congressional review provisions. The Congress adjourned on October 21, 1988. In order to satisfy section 7(o)'s waiting periods in calendar year 1988, the following types of rules would have been required to reach the following stages:

--Rule requested from the Agenda, to be published for comment: Rule must have been sent to the Banking Committees by October 7, 1988.

--Published rule to take effect: Rule must have been published by September 22, 1988.

--Interim rule requested from the Agenda, to be published for comment and for effect: Rule must have been published by September 7, 1988 (a total of 45 "session days:" 15--since the rule is to be published for public comment--and 30--since the rule is also to be published for effect).

A rule that failed to meet these dates, even by one day, would lose all its "review" days in the 100th Congress, and would have to begin again in the 101st Congress. Given the congressional schedule for the 101st Congress, the "review" periods would be satisfied as follows:

--Rule requested from the Agenda, to be published for comment: Could be published after February 7, 1989.

--Published rule to take effect: Could take effect on March 6, 1989.

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--Interim rule requested from the Agenda, to be published for comment and for effect: Could take effect on April 4, 1989.

Thus, for rules that failed to meet the applicable waiting periods in the 100th Congress by one day, the delays occasioned by operation of section 7(o) would be:

--Four months for a requested rule to be published for comment.

--Almost six months for a published rule to take effect.

--Almost seven months for a requested interim rule to take effect.

Clearly, these delays are crippling to the Department's ability to implement rule priorities. It is also worth noting that this "all or nothing" feature of section 7(o) takes its toll on all HUD regulations--including those needed to implement policy initiatives that the Congress and HUD both consider priorities.

In addition, section 7(o)'s schedule forces the Department to take into account what should be a wholly irrelevant consideration in managing its regulatory program--the congressional calendar. Rules production often turns on whether there are enough "congressional session days" to accommodate a proposed or final rule, without regard to the relative priority of the task.

The Amendment

Based on the above analysis, the Department has sought repeal of section 7(o) several times in the past. It is clear, however, that the Banking Committees continue to believe that a special tool for regulatory oversight is needed. Section 203 is the Department's response to this impasse.

This proposal would retain the legislative review framework in its entirety. However, it would eliminate the "congressional session day" as the unit of measurement for determining the length of review time to which rules are made subject.

Rules requested from a HUD agenda for review by either Banking Committee would, under the proposal, undergo review for 15 calendar days.

Any HUD rule published for effect would be required to await 30 calendar days after its publication before it could become effective. (Interim rules, as in the past, would be subject both to a 15-day prepublication review period and the 30-day waiting

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period following publication--but the periods would be measured in calendar days.)

Under current section 7(o), the 15- and 30-day waiting periods are suspended by extended congressional recesses and stopped entirely by adjournments sine die. As noted, this feature of section 7(o) has caused delays in the Department's regulatory efforts, and has distorted the Department's regulatory priorities.

The proposal would address these problems by permitting the 15- and 30-day clocks to continue running during periods of congressional absence.

The Department believes that this approach strikes a reasonable balance between the oversight needs of the Congress and the Department's rulemaking responsibilities. Congress would be provided an adequate period to review HUD rules, and the Department's rulemaking priorities would be delayed to permit this review, but would not be brought to a halt for extended periods.

There have been virtually no instances in recent years when the Congress used the legislative review process for the purpose of attempting to stop a HUD rule by formal legislative means. Most often, congressional objections to rules submitted for prepublication review are expressed informally in communications to the Department, and HUD has reacted, in the rare instances where such communications have occurred, on a case-by-case basis, depending upon the nature of the objection. Neither 15 calendar days nor 15 session days will normally be an adequate time for more than such informal communications. However, 15 calendar days--even during a recess--is enough time for a member to communicate his or her displeasure about a policy choice to the Secretary.

Similarly, the Congress can always use its influence to alter the course of HUD rules--even those published for effect--during the 30-day waiting period that the amended law would provide. The proposed revision recognizes that, whether or not the Congress is in session, committee members and their staffs are at work and are in a position to communicate with HUD any concerns they may have about a rule.

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**RATIFICATION OF THE USE OF NATIONAL COMPARABILITY
PROCEDURES FOR SECTION 8 RENTS**

Section 204 would recognize that HUD is authorized to use comparability studies in the implementation of section 8(c)(2) of the United States Housing Act of 1937. It would also expressly ratify and declare valid the interpretation that HUD has accorded section 8(c)(2) of the 1937 Act in HUD's past and continuing use of comparability studies under section 8(c)(2)(C) of the 1937 Act as an independent limitation on the amount of rental adjustments that would otherwise result from application of the annual adjustment factors (AAF) under section 8(c)(2)(A) of the 1937 Act. This section would also provide that where litigation has resulted in a judgment before the date of enactment of this section that is final and not appealable (including an order of settlement) and that is inconsistent with HUD's interpretation of section 8(c)(2), the ratification could not be used as the basis for requiring the repayment of amounts paid by HUD in accordance with the judgment or for refusal by HUD to pay amounts required by the judgment.

This section would correct the recent decision in Rainier View Associates v. U.S., 848 F.2d 988 (9th Cir. 1988), cert. denied, ___ U.S. ___, 109 S. Ct. 2065 (1989), which declared that HUD lacked authority to use comparability studies to limit adjustments under the AAF as a means of satisfying section 8(c)(2)(C)'s mandate that rents provided under section 8(c)(2) "not result in material differences between the rents charged for assisted and comparable unassisted units". The Ninth Circuit holding is contrary to the intent of the statute since it wrongfully deprives the Secretary of the discretion Congress gave the Department to determine how to implement the comparability limit in section 8(c)(2)(C) and frustrates that section's purpose by allowing project owners to receive unjustified windfall profits through rent adjustments which would raise rents above market rates. Congress has already recently reviewed section 8(c)(2)(C), and in section 142(c)(2)(B) of the Housing and Community Development Act of 1987 implicitly accepted the Department's use of comparability studies by amending the statute to allow them to be used to limit AAFs if done on a timely basis. HUD's construction of section 8(c)(2)(C) has also been a predicate for the amounts appropriated for the section 8 program.

The Rainier View judgment and related litigation have already obliged HUD to pay \$12 million in retroactive rents, and may require an added amount up to about \$3 million. HUD estimates that if the Rainier View ruling were to be applied to all affected section 8 projects within the Ninth Circuit's jurisdiction alone, the potential financial exposure for retroactive payments might amount to as much as \$200 million, and the cost of prospective rent increases over the next 10 years on

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the same basis may be another \$300 million. Moreover, HUD estimates that if the Ninth Circuit case were applied nationwide, the Federal government's potential cost would reach as much as \$1 billion for retroactive payments; and if the rationale for the case is applied in the future, it could cost an additional \$1.5 billion over the next 10 years.

This section would also statutorily provide for an appeals procedure for project owners who wish to contest the findings of a comparability study. The appeals procedure under this section is consistent with the process currently employed by HUD with the exception that project owners who have not previously appealed the findings of a past comparability study would be given a window of 30 days from date of enactment if they wish to contest the findings of that study. HUD would be required within 1 year of enactment to publish proposed regulations requesting public comment and final regulations implementing an appeals procedure for owners to contest the findings of future comparability studies.

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**TARGETING CDBG AMOUNTS TO
PERSONS OF LOW AND MODERATE INCOME**

Section 205 would amend the Community Development Block Grant (CDBG) Program under title I of the Housing and Community Development Act of 1974 to improve the targeting of CDBG assistance to persons of low and moderate income.

Existing law contains two distinct provisions dealing with the relationship between assisted activities and benefit to low- and moderate-income persons. First are the three national objectives. Each activity that a grantee funds through the CDBG program must meet one of three national objectives: benefit to low- and moderate-income persons; elimination or prevention of slums and blight; or meeting an urgent need.

Second is the extent to which assisted activities are used to benefit low- and moderate-income persons. Within the national objectives, a grantee is required to use 60% of the aggregate amounts it expends under the program -- both section 106 grants and section 108 loan guarantee proceeds -- over a one-to three-year period, as designated by the grantee, for activities that benefit low- and moderate-income persons.

The second requirement conveys the impression that at least 60% of the CDBG program's beneficiaries must be of low and moderate income. For the reasons stated below, this is not the case.

As a general rule, once an activity meets the national objective of benefiting low- and moderate-income persons, all the CDBG dollars spent on the activity are counted for purposes of meeting the 60% aggregate benefit counting requirement. An activity may qualify as meeting the national objective of benefiting low- and moderate-income persons if at least 51% of the activity's beneficiaries are low- and moderate-income persons. Thus, if a grantee spends 60% of its CDBG funds for an activity that has 51% low- and moderate-income beneficiaries, it would be credited with 60% "low/mod" benefit, even though perhaps only as low as 31% of all its funds actually benefited low- and moderate-income persons.

In certain "exception" communities (see section 105(c)(2) of the 1974 Act), an activity can qualify under the national objective of benefit to low- and moderate-income persons even if the percentage of "low/mod" beneficiaries is substantially less than 51%. Since all CDBG dollars spent on activities meeting this objective "count" toward the 60% aggregate benefit requirement, these "exception" communities can have overall programs that benefit low- and moderate-income persons even lower than the 31% figure discussed above. The lack of overall CDBG targeting is underscored by the fact that these "exception"

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communities account for 25% to 30% of all CDBG entitlement grantees.

The Department believes that these "low/mod" benefit provisions are insufficiently targeted. Particularly in this time of scarce Federal resources, the Department believes that available amounts should be directed more fully to those who need them most -- low- and moderate-income persons. The proposal seeks to accomplish this end in three ways.

First, the proposal would increase from 60% to 75% the percentage of CDBG amounts -- section 106 grants and section 108 loan guarantee proceeds -- that must be used to benefit low- and moderate-income persons. This increase would recognize the overall need to more tightly target CDBG amounts to benefit low- and moderate-income persons, while still providing a measure of discretion in selecting activities to be carried out for this purpose.

Second, the proposal would require that all activities carried out by more affluent units of general local government benefit low- and moderate-income persons. Thus, these communities could not carry out CDBG activities that are designed to prevent or eliminate slums or blight or to meet urgent needs. This element of the proposal recognizes the fact that more affluent communities are in a better position to meet the community and economic development needs of their wealthier constituents: for these communities, all CDBG activities would have to meet the national objective of benefit to low- and moderate-income persons.

The second change would not affect "severely distressed" communities. Activities carried out by these communities would continue to be directed to any of the three national objectives, subject, of course, to the 75% "low/mod" benefit requirement described above. This reflects the fact that severely distressed units of general local government do not have sufficient local resources to provide for their community and economic development needs, and require greater flexibility in developing their CDBG programs.

Two types of units of general local government could be considered severely distressed for purposes of this amendment:

-- Those for which a major disaster is declared, in accordance with 42 U.S.C. 5121 et seq., and that meet such other standards as the Secretary may determine; or

-- Those that meet the minimum standards established by the Secretary for measuring the capacity of units of general local government to meet the needs of low- and moderate-income persons with their own resources.

Both of these standards would be contained in a regulation promulgated by the Secretary after notice and opportunity to comment.

The proposal's third element would change how program funds spent by grantees are credited for purposes of meeting the requirements that a minimum percentage of funds must be spent for low- and moderate-income persons. The amount of CDBG funds expended on most activities would be discounted to reflect only the extent to which the beneficiaries of such activities are comprised of low- and moderate-income persons. With the exception of activities involving the acquisition, construction, or improvement of property for housing, for purposes of meeting the 75% overall benefit requirement, the amount of program funds spent on an activity that does not exclusively benefit low- and moderate-income persons would be discounted to the degree that the percentage of low- and moderate-income persons benefiting from the activity falls short of 100%.

For example, consider a grantee's expenditure of \$100,000 on an economic development activity that creates 10 new jobs, seven of which are taken by low- and moderate-income persons. Under the current statute and regulations, all \$100,000 would be credited towards meeting the grantee's 60% overall expenditure requirement. Under the proposed approach, only 70% of the \$100,000 (based on seven out of 10 jobs), or \$70,000, would be credited towards meeting the new 75% overall benefit requirement. In order to raise the overall spending level to a minimum of 75% this grantee would need to spend an amount at least equal to \$100,000 on another activity benefiting persons 80% or more of whom are low- and moderate-income persons.

Because of the national policy of attempting to avoid the undue concentration of low- and moderate-income persons geographically, an exception would be made for housing activities that are assisted with CDBG funds. Full credit for such expenditures would be given in any case where the proportion of units in the assisted housing that will be occupied by low- and moderate-income persons is at least equal to the percentage of the total cost of the activity that is contributed by CDBG funds.

HUD expects that many entitlement communities and States will not have to make adjustments to their selection of activities or, for States, their method of distribution to comply with these new requirements. Others would need to make relatively minor changes. However, HUD recognizes that for some communities and States these requirements would necessitate quite substantial modification to meet these targeting requirements.

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An example of a grantee's annual program of activities would help illustrate how the proposed system would operate, and how it would differ from the system currently in place:

Grantee "A's" Annual Program of Activities totalling \$500,000

- \$100,000 Rehabilitate a recreation center serving a neighborhood having 30% low/mod income residency. (This would qualify as benefiting low/mod income persons assuming this community qualifies for the area benefit exception discussed above.)
- \$150,000 Loans to low/mod income elderly homeowners for emergency home repairs.
- \$100,000 Acquisition of land to be donated to a nonprofit housing developer on which the nonprofit will develop a 20-unit structure for rental housing for large families, five units of which will be held for occupancy by low- and moderate-income households at affordable rents. Total development costs are expected to be \$1,000,000.
- \$100,000 Loan to a for-profit business to enable expansion, creating 10 new jobs, six of which will be held for low/mod income persons.
- \$ 50,000 Facade improvements for blight removal in a small business district located in a residential area having 40% low/mod income residency.

Determining the Overall Benefit Percentage

| <u>Activity</u> | <u>Overall Benefit Using</u> | <u>Overall Benefit</u> |
|---------------------------------|-----------------------------------|---------------------------------|
| | <u>Current Counting Procedure</u> | <u>Based on Proposal</u> |
| Recreation Center | \$100,000 | \$ 30,000 |
| Homeowner Loans | 150,000 | 150,000 |
| Rental Housing Land | 100,000 | 100,000 |
| Business Loan | 100,000 | 60,000 |
| Blight Removal | <u>- 0 -</u> | <u>20,000</u> |
| Total Low/Mod Income Benefit | \$450,000 | 360,000 |
| Overall Benefit Percent | <u>450,000</u> 500,000 = 90% | <u>360,000</u> 500,000 = 72% |

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Note that the land acquisition for large family rental housing receives full credit under both the existing and proposed approaches, even though the project will only have low/mod income occupancy of 25%. This is because the CDBG contribution of \$100,000 represents only 10% of the total project development costs, well below the 25% expected occupancy level of low- and moderate-income persons. Through the use of this exception, we aim to encourage a balancing of income levels among occupants of multi-unit housing projects. It should also be noted that, under the proposal, credit can be given for an activity that is carried out under the slums/blight and urgent needs objective in certain circumstances. While the number of communities that would be eligible to carry out activities under those objectives would be limited to those that are distressed, this could still be an important consideration for helping them to meet the overall 75% low/mod benefit level requirement.

Finally, the proposal contains a transition provision. The amendments made by the proposal would take effect upon enactment of this Act. Some units of general local government will, as noted earlier, have one or more years remaining on the time periods they designated for fulfilling the 60% "low/mod" benefit requirement of current law. These communities would be given an option: they can forego the remaining time and immediately switch to a new time period for implementing the new system by designating a new time period, or they can choose to remain with the old time period. In either event, the grantees would be required to comply with all of the requirements of this proposal upon their enactment.

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CDBG ANTIPOVERTY STRATEGY

Section 206 would require each Community Development Block Grant grantee to certify, as a condition of receiving a grant, that it is following an antipoverty strategy which has been approved by HUD. The antipoverty strategy would:

(a) embody a plan that would provide housing, economic development, and social service resources to persons who are living in poverty and that, to the greatest extent possible, would involve close cooperation with community-based organizations comprised of low-income persons and others who have a stake in the community and with agencies providing assistance to low-income persons;

(b) estimate the number of people in the community or the nonentitlement areas of the State who are living in poverty, identify the principal areas and conditions in which they live, and explain the basis for this information;

(c) identify existing facilities, resources, and public and private organizations that are or could be used to address the needs of those living in poverty, and funding that could be used; and

(d) set forth a strategy for coordinating CDBG activities (or the method of distribution by States) with facilities, resources, organizations, and funding identified under paragraph (C);

Grantees would adopt their antipoverty strategies only after giving citizens or, in the case of States, units of general local government an opportunity to comment on the proposed strategy. The actions that apply to the development of statements of projected use of funds (or State methods of distribution) would also apply to the development of antipoverty strategies.

HUD would approve the strategy unless it is incomplete, the needs or conditions identified are plainly inconsistent with generally available facts or data, or the strategy for the use of CDBG funds is plainly inappropriate to address the identified needs.

This proposal would bring CDBG grantees into partnership with HUD as it wages a new war on poverty and would require them to think through a CDBG strategy consistent with Federal goals.

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SYNTHESIS OF BLOCK GRANT SANCTIONS

Section 207 would synthesize the statutory sanctions under the community development block grant legislation to conform explicitly to a recent judicial decision and to facilitate the exercise of these sanctions by HUD in an effective and equitable manner.

HUD's longstanding implementation of section 104(e) (to be redesignated as section 104(f) by section 206) and section 111 of the block grant statute was challenged in Kansas City v. HUD, 861 F.2d 739 (D.C. Cir. 1988). The Department's administration of the CDBG program had utilized a method of conditioning contracts to obtain improved performance by grantees. The court held that at least in some instances the full-scale administrative hearing provided for in section 111 must be furnished before a grant can be conditioned.

From virtually the beginning of the block grant program, HUD had taken the position that section 104 constituted authority to make adjustments, including potential adjustments by means of conditioning annual grants, for grants yet to be approved. It considered section 111, with its more detailed procedural requirements, to be applicable to any attempt by the Department to impose mandatory sanctions against grants that had been unconditionally obligated by the Department.

The distinction drawn by HUD, and contained in its regulations for more than a dozen years, was itself a reflection of the ambivalence in the statute between these two provisions. Section 111 was the vestige of the hands-off special revenue sharing-type approach proposed by the Nixon Administration in 1973; section 104(e) was a more hands-on, post-audit enforcement tool added by the Congress. From the beginning, the two provisions had a substantial overlap in that both covered instances of noncompliance. But the Court in Kansas City v. HUD found HUD's implementation wanting. Rather than applying the sanctions respectively to whether the grant was already made or yet to be made, the court ruled that section 111 applied to all cases involving past substantial noncompliance by the grantee. The Department is now following the ruling in Kansas City, as well as the corollary authority to continue to condition upcoming grants for cases in which the performance problem is ongoing.

This amendment would update the legislation by expressly tying section 111 remedies to cases of past substantial noncompliance and section 104(e) to cases in which the performance problem is continuing. Further, the amendment would make clear the range of the Department's administrative hearings under section 111 in cases of past substantial noncompliance. This amendment would state expressly that the Department could exercise the sanctions in section 111 under an administrative

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hearing with regard to grants already made or to be made. The independent authority under section 111 to refer cases of substantial noncompliance to the Attorney General would be retained. Moreover, under this authority the Attorney General may seek money damages (which are not limited to the previously provided grants), as well as mandatory or injunctive relief.

Correspondingly, section 104 would also be revised to recognize expressly that the Department can undertake funding sanctions with respect to grants already made or to be made, but limited exclusively to cases of continuing performance problems. Any such sanctions, including conditioning, could only be imposed after the Secretary provided the grantee a reasonable opportunity for informal consultation.

This proposal aims to integrate the Kansas City decision in a programmatically efficient manner within the context of the original block grant legislation's separate remedies at sections 104 and 111.

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NULLIFICATION OF RIGHT OF REDEMPTION OF SINGLE FAMILY MORTGAGORS UNDER SECTION 312 REHABILITATION LOAN PROGRAM

Section 208 would preempt State laws giving section 312 single family mortgagors a right to redeem their properties after foreclosure. Under State redemption statutes, mortgagors have a specified period of time to make payment on the foreclosed property and regain title. Subsection (a) applies to situations in which HUD or its foreclosure agent forecloses on its Section 312 loan, and subsection (b) applies to situations in which HUD buys in a property at the foreclosure sale of a mortgagor having a lien senior to HUD's section 312 loan mortgage. Under subsection (a), the foreclosure sale to any purchaser nullifies the right of redemption of the mortgagor. In the subsection (b) situation, the mortgagor's right of redemption will be nullified by the sale to HUD, and HUD may subsequently sell the property free of this encumbrance.

Preempting State redemption laws for section 312 single family properties would permit the Department to sell these properties under this section at foreclosure sale, or following a buy in, in the same expeditious manner as HUD-held single family properties under the FHA single family mortgage insurance program.

There is considerable legislative precedent for this section. Section 569 of the 1987 Act added section 204(1) to the National Housing Act to provide that when HUD forecloses on a HUD-held mortgage secured by a single family property, the purchaser at the sale is entitled to receive immediate title to the property, notwithstanding any State law granting redemption rights to the mortgagors. This provision is analogous to proposed subsection (a) cases where HUD forecloses. (A provision analogous to proposed subsection (b) that would apply to FHA single family mortgages is not necessary since FHA takes only first lien positions.) The right of redemption had earlier been nullified for all Secretary-held multifamily foreclosures (under both the National Housing Act and section 312), under the Multifamily Mortgage Foreclosure Act of 1981.

The various State laws which govern foreclosures pose several problems. During the lengthy periods of time required to foreclose (and provide redemption) under some State laws, the properties deteriorate and are subject to vandalism and fire loss, because they are vacant. The locations of section 312 properties tend to be in more urbanized, less affluent areas, where vacant properties tend to degrade faster, and where there may be a better opportunity for local government to use the property in an Urban Homesteading program. Vacant, deteriorating properties adversely affect the neighborhoods and communities in which they are located. Further, while the properties are in a "limbo" state due to redemption delays, they are being lost to

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the national stock of livable housing. Legislation preempting State redemption statutes can diminish these problems by reducing the amount of time it takes to foreclose, and then dispose of the property for reuse. The delay serves no purpose but to frustrate HUD's disposition efforts and the immediate occupancy of the building, since it is very rare that mortgagors redeem section 312 properties.

TITLE III -- FEDERAL HOUSING ADMINISTRATION REFORM**ANNUAL FINANCIAL STATEMENTS**

Section 301 would require the Secretary to make available to the public each year an audited financial statement of the insurance funds established under the National Housing Act beginning with fiscal year 1989. The statement would be required to present the financial condition of the funds on both a cash and accrual basis, consistent with generally accepted accounting principles (GAAP). Each financial statement would be audited by an independent accounting firm selected by the Secretary.

Annual audited financial statements are the most basic of all management requirements. In a financial operation, these comprehensive financial reports drive decisions that affect all lower level systems. The systems deteriorate without the discipline of rigorous annual review by senior management.

From 1974 to 1989, FHA's finances were not audited by an outside accounting firm. This meant that, for 15 years, public accountability was limited. The General Accounting Office (GAO) attempted audits in 1981 and 1984, but FHA's books were in such disarray that the preparation of financial statements was impossible. In 1987, GAO began again, this time spending two years working with Price Waterhouse and HUD's Office of Finance and Accounting to develop systems capable of measuring the agency's finances.

On September 27, 1989, GAO's Comptroller General reported to Congress that full financial statements for FHA had been completed. These statements showed a \$4.2 billion accrual basis loss in FY 1988. FHA had reported a \$856 million loss for the same period on a cash basis. The difference in these two amounts was due to the large number of defaults and delinquencies that occurred in 1988 but did not result in a claim paid by FHA. FHA's managers had an unrealistically rosy picture, because claims were only counted when they were paid, not when the default or delinquency occurred. FHA will have to pay these claims over the next several years.

Requiring annual audits of the funds on an accrual, as well as a cash, basis will, for the first time, give the Department, the public, and Congress a clear and unbiased picture of the financial status of FHA's programs. This will permit HUD to adjust its programs, inform Congress, and take other appropriate steps if serious imbalances in the funds develop.

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ELIMINATION OF PRIVATE INVESTOR-OWNERS FROM THE FHA SINGLE FAMILY MORTGAGE INSURANCE PROGRAM

Section 302 would eliminate private investor-owners from participation in FHA's single family mortgage insurance programs. FHA's single family insurance programs should be designed to provide homeownership opportunities for families that will occupy their own homes. FHA should not exist to provide profit opportunities to private investors. Investors are much more likely to walk away from their homes in an economic downturn and are responsible for the majority of the fraudulent schemes in FHA programs.

Investors are only a small portion of FHA's business, but a significant source of its financial difficulties. In 1988, investors accounted for only 2.5% of FHA's newly insured mortgages, and roughly 15% of the claims. Most of the defaulting loans were written in earlier years. One group of private investors in Denver owned 750 homes with insured mortgages, and defaulted on every one of the mortgages.

Under the proposal, private investors would be excluded from FHA insurance of single family homes that they do not occupy. Still accepted would be public purpose investors, such as nonprofit housing providers that intend to rent or sell the homes to low- and moderate-income persons and State and local housing finance agencies. Multi-unit, owner-occupied structures would continue to be permitted, as for example, a family occupying one unit of a duplex while renting out the other.

By this proposal, HUD is not seeking to discourage private investment in housing as a general matter. The reform is rather a recognition that the single family mortgage insurance program should not be exposed to the risks of private speculation.

The amendments made by this proposal are prospective only. They would apply only with respect to --

(1) mortgages insured --

(A) pursuant to a conditional commitment issued on or after the date of the enactment of this Act; or

(B) in accordance with the direct endorsement program (24 CFR 200.163), if the approved underwriter of the mortgagee signs the appraisal report for the property on or after the date of the enactment of this Act; and

(2) the approval of substitute mortgagors, if the original mortgagor was subject to the amendments.

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In addition, any mortgage insurance provided under title II of the National Housing Act, as it existed immediately before the date of the enactment of this Act, would continue to be governed (to the extent applicable) by the current provisions of the National Housing Act, as they existed immediately before such date.

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**REQUIRE CREDIT REVIEWS OF PERSONS ACQUIRING
FHA MORTGAGED PROPERTIES FOR LIFE OF MORTGAGE**

Section 304 would amend section 203(r)(2) of the National Housing Act (NHA) to require lenders to review the creditworthiness, under standards prescribed by HUD, of at least one person seeking to acquire ownership of a one- to four-family residential property encumbered by an FHA mortgage at any time during the life of the mortgage, whether or not such person assumes personal liability under the mortgage (except that acquisitions by devise or descent shall not be subject to this requirement). Section 203(r)(2) currently requires reviews of the credit standing of persons seeking to acquire a property encumbered by an FHA mortgage (1) during the 12-month period following execution of the mortgage, or (2) in the case of an investor-originated loan, during the 24-month period following execution.

This proposal would also permit HUD to require each insured mortgage to contain a due-on-sale provision permitting the mortgagee to accelerate the period of time in which a mortgage obligation is due and require repayment of that obligation. Under the proposal, the due-on-sale provision would not be subject to section 341(d)(6) of the Garn-St Germain Depository Institutions Act of 1982. Section 341(d)(6) prohibits the exercise of a due-on-sale provision upon a transfer where the spouse or children of a mortgagor become an owner of the property.

Before enactment of the Housing and Community Development Act of 1987, there was no statutory requirement to verify the creditworthiness of persons seeking to acquire properties encumbered by FHA mortgages. Consequently, defaults by unqualified homebuyers of properties encumbered by FHA mortgages were a costly drain on the FHA mortgage insurance fund. In particular, properties were often sold to investors who made few, if any, home improvements and who then sold the properties to unqualified homebuyers. Many of these buyers subsequently defaulted on the properties while the lenders received mortgage insurance benefits.

The 1987 Act partially remedied this situation by requiring credit checks of any person seeking to acquire a property burdened by an FHA mortgage (1) during the 12-month period following execution, or (2) in the case of investor-originated loans, during the 24-month period following execution. Defaults by unqualified homebuyers, who purchase properties encumbered by FHA mortgages after the 12- and 24-month time periods, still expose the FHA mortgage insurance funds to unjustified losses. The amendment to section 203(r) would further reduce claims on the FHA insurance funds by ensuring that, at any time during the

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life of the mortgage, at least one person seeking to acquire property encumbered by an FHA mortgage is creditworthy.

By providing an exemption from section 341(d)(6) of the Garn-St Germain Depository Institutions Act of 1982 to section 203 of the NHA, non-creditworthy relatives would be prevented from acquiring properties encumbered by FHA mortgages. Such transfers are a major method of avoiding application of credit reviews, since the assumption restriction is implemented by including a due-on-sale provision in the mortgage which allows acceleration of the loan upon transfer to a noncreditworthy person. This proposal would also make explicit HUD's authority to require each insured mortgage to contain a due-on-sale provision.

This amendment would also amend the first sentence of section 203(r) to provide that the actions HUD takes under this section to reduce losses applies to all single family programs under title II of the NHA.

Section 203(r)(3) currently requires that the original mortgagor be advised of the procedures for release of liability only if the mortgage is assumed after the 12- and 24-month periods specified in section 203(r)(2). This section contains a technical amendment to section 203(r)(3) which removes the reference to the 12- and 24-month periods of time. Under this amendment, in any case where personal liability under a mortgage is assumed, the original mortgagor would have to be advised of the procedures by which he or she may be released from liability.

The amendments made by this proposal are prospective only. They would apply only with respect to --

(1) mortgages insured --

(A) pursuant to a conditional commitment issued on or after the date of the enactment of this Act; or

(B) in accordance with the direct endorsement program (24 CFR 200.163), if the approved underwriter of the mortgagee signs the appraisal report for the property on or after the date of the enactment of this Act; and

(2) the approval of substitute mortgagors, if the original mortgagor was subject to such amendments.

In addition, any mortgage insurance provided under title II of the National Housing Act, as it existed immediately before the date of the enactment of this Act, would continue to be governed (to the extent applicable) by the current provisions of the

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National Housing Act, as they existed immediately before such date.

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REPEAL OF TITLE X

Section 305 would repeal title X of the National Housing Act.

Prior Suspension and Proposed Termination of Title X Program

On June 29, 1989, Secretary Kemp announced HUD's suspension of the title X program. He announced that HUD would discontinue the processing of title X applications that had not received a legally binding commitment by June 29, 1989, and would return application fees. Projects with legally binding commitments issued before June 29, 1989 would be eligible for insurance, subject to a specific examination for evidence of fraud or misrepresentation. On August 11, 1989, HUD published a rule proposing to terminate the program (54 Fed. Reg. 33.039).

Background

Title X of the National Housing Act was added by the Housing and Urban Development Act of 1965. Under this program, HUD is given discretionary authority to insure mortgages for land purchase and development in connection with new subdivisions and new communities. The improvements that may be installed by the developer and financed with the mortgage proceeds include: installations for water lines; water supply; sewage disposal; complete water or sewage systems; and roads, streets, curbs, gutters, sidewalks, and storm drains. Title X projects must be designed for primarily residential use, although a reasonable amount of related nonresidential use is permitted.

Termination of the title X program is being proposed on the basis of the following factors: the serious adverse financial condition of the program, its inability to meet its statutory goals, the Secretary's judgment that restructuring the program would not be an effective way of correcting these deficiencies, and the fact that its termination would have virtually no effect on the availability of financing for land development across the nation. The following discussion addresses each of these points.

1. Financial Condition of the Title X Program

Title X has proved to be a financial disaster to the Department and to the American people. The program has experienced exceptionally high claim rates, and it has already inflicted massive losses on the Department's insurance fund, with substantial additional losses anticipated. The program is actuarially unsound, a situation that is particularly troublesome since it involves a program that is intended to be self-supporting (see section 1008 of the National Housing Act).

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An analysis of the operations of the program from 1977 to October 1988 reveals the following:

- Fifty-eight loans were insured under the program (approximately five per year). These mortgages generated \$12.5 million in insurance premiums and fees for the fund and were insured for a total of \$505,148,309 (approximately \$8.7 million per loan).

- Claims have been paid on 25 of the 58 loans. This represents a claim rate of 43%. As a point of comparison, the claim rate for the section 221(d) multifamily mortgage insurance program for the period 1974 through 1988 was 9.87% for HUD-processed loans and 17.31% for the section 221(d) coinsurance program.

- By October 1988, 13 of the 25 title X projects for which HUD has paid claims since 1977 have been sold, resulting in a total loss to the Federal government of more than \$50 million and an average loss of almost \$4 million per claim. Losses on the remaining 12 projects have not, as yet, been determined. However, assuming comparable losses upon the disposition of these projects, HUD anticipates a total loss on the 25 claims of approximately \$90 million. The ultimate loss will exceed \$90 million, since HUD has issued legally binding commitments for a number of projects that are still in the pipeline.

- HUD has experienced no significant reduction in title X financial problems despite a number of changes that were instituted between 1983 and 1985 to improve the program.

- The Federal government's future losses under the program can only be expected to increase if the program is allowed to continue, since the amounts sought to be insured under individual title X applications are increasing.

Consequently, HUD believes that title X projects will continue to subject the FHA insurance fund to unacceptable financial losses. The continuation of a program that involves such an unacceptably high insurance claim rate is inconsistent with the Department's obligation to manage the FHA insurance fund prudently.

2. Inability to Promote Statutory Purposes

The statute mandates the inclusion of a proper balance of housing for families of low and moderate income (section 1005). However, HUD has been unable to achieve this goal.

The HUD Inspector General draft audit report dated March 31, 1987 reviewed 17 title X projects in three HUD regions that produced 11,300 housing units. These projects collectively were

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insured for a total of \$212 million. The review revealed that only a single project may have provided housing for moderate-income persons, and no project provided housing for families with low incomes.

Housing located on land developed under the program is typically new construction that is designed for sale to prospective homeowners. This type of housing generally costs more than low-income families, and even many moderate-income families, can afford to pay. In addition, undeveloped land suitable for use in the program is generally located in suburban areas, and involves an "upscale" emphasis that is often beyond the reach of even moderate-income families. Thus, the central thrust of title X is away from the very income groups the statute directs the Department to focus upon in administering the program.

3. Restructuring Title X Would Be Ineffective

The private sector currently finances virtually all land development projects without the need for Federal insurance. The Department estimates that between 4,000 and 6,000 subdivisions are developed annually in the United States. By comparison, activity under the title X program since 1977 has averaged only five applications per year. In other words, title X's share of the land development market has averaged only about 0.1% of the national total -- an infinitesimal contribution to the total financing for land development.

The Department believes that restructuring the title X program would result in reducing the current five applications per year to zero. Any restructuring of the program would include more rigorous requirements to ensure the participation of small builders and a significant proportion of low- and moderate-income families in the housing ultimately developed. It also would involve stricter underwriting standards and other measures to ensure that insured projects represented a substantially improved mortgage insurance risk. Such changes would virtually end any developer interest in the program. Thus, the only viable approach is to terminate the program.

4. Effect on the Availability of Financing for Land Development

Finally, the termination of title X would have virtually no effect on the availability of financing for land development across the Nation. As indicated above, the private sector finances the overwhelming number of land developments, with title X's share of the market being negligible.

For these reasons, this proposal would terminate the title X program.

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Effective Date and Conforming Amendments

No contract of insurance could be entered into under title X on or after the date of enactment, except pursuant to a commitment to insure made before enactment. Any contract of insurance entered into under title X would continue to be governed by title X as it existed before repeal. In view of the suspension of the title X program on June 29, 1989, it is not necessary to provide a transition period.

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**STREAMLINE PROPERTY DISPOSITION REQUIREMENTS
FOR UNSUBSIDIZED MULTIFAMILY HOUSING PROJECTS**

Section 306 would amend sections 203(a) and (d) of the Housing and Community Development Amendments of 1978 to (1) permit HUD to use either tenant-based (vouchers or certificates) or project-based section 8 assistance for units in unsubsidized projects which are occupied by lower income families; and (2) remove the requirement that HUD provide section 8 assistance for the vacant units in such projects. To use tenant-based section 8 assistance, HUD would have to make a determination that there is available in the area an adequate supply of habitable, affordable housing for lower income families. Such a determination would be final and nonreviewable. This determination is the same standard used for similar purposes in connection with the CDBG antidisplacement plan under section 104(d) of the 1974 Act.

Section 203(d) of the 1978 Amendments currently requires HUD (1) to provide 15-year project-based section 8 assistance to multifamily projects that are acquired at a HUD foreclosure or after sale by HUD, or (2) to ensure that for at least 15 years eligible tenants will pay no more in rent than if section 8 were provided. The assistance is required for (1) all units in subsidized or formerly subsidized projects, (2) the units in other (unsubsidized) projects owned by HUD that are occupied by lower income families or are vacant, and (3) the units in all other (unsubsidized) projects that are occupied by lower income families.

This amendment would give HUD needed flexibility to use tenant-based assistance, instead of project-based assistance, in unsubsidized projects where local market conditions clearly indicate that the project is not needed to be maintained to provide lower income housing. HUD could make a determination in soft market areas that there is available an adequate supply of habitable affordable housing for lower income families. Therefore, if the project were not used for lower income purposes following the sale, the lower income tenants receiving the section 8 assistance would be able to find affordable housing in the area. Roughly half of the projects owned by HUD or for which HUD is mortgagee in possession (53 projects and 8,000 units) are located in the soft market areas of Texas, Oklahoma, Louisiana, and Arkansas. HUD would still be required to provide project-based assistance to all units in subsidized projects or formerly subsidized projects.

This amendment would also remove the requirement that HUD provide section 8 assistance for vacant units in unsubsidized projects sold by HUD. This requirement exposes HUD to a significant obligation of budget authority. It is estimated that there are more than 3,000 vacant units potentially eligible for

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this assistance, which would represent between \$300 to \$400 million in budget authority. Obligation of this budget authority for vacant units alone is especially questionable since many of the units are in soft markets where, as discussed above, local market conditions indicate projects do not need to be maintained as lower income housing.

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PROHIBIT DEALER AND LOAN BROKER PARTICIPATION IN ORIGINATION OF TITLE I PROPERTY IMPROVEMENT LOANS

Section 307 would amend section 2 of the National Housing Act to prevent certain abuses that have developed under the title I property improvement loan program involving loans originated with the participation of dealers and loan brokers.

Currently, some property improvement dealers or contractors assist their customers in completing and submitting title I property improvement loan applications for the work they do. This is done pursuant to agreements that the dealers have with the financial institutions which finance the loans. Under current statutory authority, financial institutions can purchase advances of credit (retail installment sales contracts with the borrowers) from the dealers.

Some dealers have abused this arrangement by encouraging borrowers to inflate their incomes and/or hide their debts, thereby giving the appearance that the borrowers are creditworthy and qualified for property improvement loans.

Section 2(b)(8), as added by this section, would remove the Secretary's authority to insure advances of credit under the property improvement loan program. The effect of this section is that a borrower would have to apply directly to a lender for his or her loan, and the dealer would have no role in the loan origination process. This would eliminate the dealer's inherent incentive to do what it can to have the financing approved so it can make the sale.

Another area of abuse involves loan brokers. A loan broker assists borrowers in obtaining title I financing for property improvements. A loan broker often works for more than one lender, and has no incentive to obtain the best deal for the borrower; in many cases the loan broker's commission is higher if the borrower pays a higher interest rate. Some loan brokers have advised borrowers that title I property improvement loan proceeds could be used for ineligible items, including swimming pools, and ineligible uses, such as paying for personal expenses and consolidating debts. One loan arranged through a loan broker was used to finance the borrower's divorce, even though the application stated that the loan proceeds would be used for home improvements. A loan broker has essentially the same incentive as dealer, to do what the broker can to have the financing approved, even for a borrower who is not creditworthy, so that the broker can earn a commission from the making of a loan.

Section 2(b)(7), as added by this section, would require financial institutions making title I property improvement loans to certify to the Secretary that no loan broker or other party having a financial interest in the making of the loan or advance

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of credit provided assistance to the borrower in preparing the loan application or otherwise assisted the borrower in obtaining the loan or advance of credit. Advances of credit are included in this provision, notwithstanding the revocation of the Secretary's authority to insure them contained in section 2(b)(8) because the certification would be required immediately upon enactment, whereas the revocation of the authority to insure advances of credit would become effective 90 days after enactment.

A BILL

To amend provisions of the Bankruptcy Code governing the powers of a bankruptcy court and the effect of automatic stays as they relate to certain multifamily liens insured or held by the Secretary of Housing and Urban Development or the Secretary of Agriculture, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That
section 105(b) of title 11 of the United States Code is amended to read as follows:

"(b) Notwithstanding subsection (a) of this section, a court may not:

"(1) appoint a receiver in a case under this title; or

"(2) issue any order, process, or judgment that operates as a stay of any of the acts excepted from automatic stay pursuant to section 362(b)(8)."

SEC. 2. Section 362(b)(8) of title 11 of the United States Code is amended to read as follows:

"(8)(A) under subsection (a) of this section, of any act by the Secretary of Housing and Urban Development or the Secretary of Agriculture included under subparagraph (B) relating to property that:

"(i) includes five or more living units and that is subject to a lien insured or held by the Secretary of Housing and Urban Development, including a lien held

in the name of the United States of America acting by and through the Secretary of Housing and Urban Development;

"(ii) includes five or more living units that are subject to a lien insured or held by the Secretary of Agriculture pursuant to title V of the Housing Act of 1949;

"(iii) is subject to a lien insured or held by the Secretary of Housing and Urban Development pursuant to title X of the National Housing Act, as it existed immediately before the effective date of the Department of Housing and Urban Development Reform Act of 1989;

"(iv) is a hospital or nursing home and that is subject to a lien insured or held by the Secretary of Housing and Urban Development; or

"(v) is subject to a lien under section 312 of the Housing Act of 1964, except a lien on property or a combination of property with up to, and including, four living units, which property has no commercial space.

"(B) The acts of the Secretary of Housing and Urban Development or the Secretary of Agriculture referred to in subparagraph (A) include --

"(i) the commencement, continuation, or completion of any act or proceeding by either Secretary for obtaining and applying cash collateral; for

obtaining possession pursuant to contract with the debtor or otherwise; for appointment of a receiver; for foreclosure of a mortgage or other lien; or for sale and conveyance of title to real or personal property; or

"(ii) any other act to protect the financial position or interest of either Secretary, which act is authorized under any applicable contract, regulatory agreement, regulation, or statute.".

SECTION-BY-SECTION EXPLANATION AND JUSTIFICATION

Exemption of HUD and FmHA Multifamily Loan
Foreclosures and Related Actions from the Bankruptcy Code

This bill would amend sections 105 and 362 of the Bankruptcy Code (title 11 of the United States Code, as recodified by the Bankruptcy Reform Act of 1978 (Pub. L. 95-598; 92 Stat. 2549)). The changes to section 362 would exempt from the automatic stay provisions of the Bankruptcy Code those acts taken by the Secretary of HUD or Agriculture toward foreclosure (including acts to obtain possession or for the appointment of a receiver) on multifamily projects with liens that are insured or held by the Secretary of Housing and Urban Development, or by the Secretary of Agriculture pursuant to title V of the Housing Act of 1949. Other acts to protect the financial position or interest of the Secretaries in bankruptcy situations relating to these projects would also be excluded from the automatic stay where a right (for example, to offset funding otherwise due to a debtor) is provided for under contract, regulatory agreement, regulation, or statute. The amendments to section 105 would make clear that the acts covered by these changes to section 362 are not subject to a bankruptcy court's discretion to issue stay orders.

This proposal requests restoration of the HUD position under sections 663 and 917 of the old title 11 (repealed in 1978), which provided relief from the automatic stay for multifamily projects insured under the National Housing Act. In addition to this restoration, the proposal would accord relief from the automatic stay for projects under the section 312 rehabilitation loan multifamily program; for land development projects under title X of the National Housing Act, as it existed immediately before the effective date of the "Department of Housing and Urban Development Reform Act of 1989" (since the 1989 Reform Act would repeal title X); for multifamily projects under section 202 of the Housing Act of 1959; for hospitals and nursing homes under sections 242 and 232, respectively, of the National Housing Act; and for any other projects with mortgages held or insured by HUD under existing or now-dormant programs. It would also accord such relief for the Secretary of Agriculture under the multifamily program of the Farmers Home Administration (FmHA) in the Department of Agriculture.

Section 362(a) of the current Bankruptcy Code states the general rule that once a bankruptcy petition has been filed, there is an automatic stay imposed on the commencement or continuation of judicial, administrative, or other proceedings against a debtor. Section 362(b)(8) provides a narrow exception to the automatic stay rule, permitting the Secretary of HUD to commence foreclosure on a mortgage or deed of trust which is insured or was formerly insured under the National Housing Act,

is held by the Secretary, and covers property or a combination of property consisting of five or more living units. The section 362(b)(8) exception, however, is considerably more restrictive than the analogous provision under the old Bankruptcy Act, and is too narrow to be fully effective in the protection of the FHA insurance fund and the tenants of HUD-insured or -assisted multifamily housing projects from the potentially adverse impact of mortgagor bankruptcies. An expansion in the terms of the exception would be desirable for the following reasons.

The great majority of mortgagor-participants in HUD-insured or HUD-assisted multifamily housing projects are limited partnerships formed for the purpose of providing investor tax shelters. Defaults on mortgage obligations frequently reflect the financial incapacity of the mortgagor properly to manage and maintain the insured property. Defaults often lead to foreclosure. If the mortgagor declares bankruptcy, however, this will delay the foreclosure. Once in bankruptcy, the delinquent mortgagor has the positive tax advantage of continuing to take depreciation deductions, as well as other permissible deductions under the accrual method, without making mortgage payments. Under current law, HUD can commence foreclosure proceedings, but cannot prosecute them further. Moreover, in such situations, HUD may be stayed from protecting the Federal financial interests by taking such actions as off-setting with funds otherwise due a debtor. Prosecution of a foreclosure and other actions are thus delayed by the bankruptcy, to the detriment of the Federal government's financial interests and to the potential disadvantage of tenants -- many of them low- and moderate-income persons -- stemming from the physical deterioration of the affected projects.

To remedy this situation, the proposal would expand the existing exception to the automatic stay provisions in two respects. First, since the existing exception applies only to the commencement of a foreclosure action, the automatic stay still applies to any other step in the prosecution of a foreclosure, once commenced, and owners and their investors continue to enjoy the tax advantages until the automatic stay is lifted and the government's foreclosure action is completed. Therefore, the proposal would permit prosecution of further steps, through the completion of foreclosure.

Second, because only the commencement of foreclosure actions is now exempt from the automatic stay provisions, actions to obtain possession as a mortgagee in possession or for the appointment of a receiver, or otherwise to protect the Federal financial interest, cannot be pursued. Pending a determination of whether foreclosure is necessary, it is highly desirable for the HUD Secretary to have these options, both for the protection of the FHA insurance funds and to protect tenants by assuring

continued, satisfactory management and operation of multifamily housing projects in default. In this regard, the longer a property is tied up in bankruptcy, the more physical deterioration is likely and the greater is the need for intermediate remedies, such as receivership. Moreover, the longer the bankruptcy proceedings last, the more sharply reduced the proceeds of sale are likely to be, when finally permitted after foreclosure. (This problem is particularly serious for properties with section 312 rehabilitation loans, since these loans typically have a junior position among the liens on the property.)

In addition, the proposal would amend section 105 of the Bankruptcy Code, to prevent a bankruptcy court from invoking its other discretionary powers in a way that would frustrate the purposes of expanding the exemption from section 362's automatic stay. The central concern is that unless section 105 is amended, section 362(b)(8) (even as amended under the proposal) would not necessarily protect the Secretaries of HUD and Agriculture, since a bankruptcy court could make injunctive or other equitable relief available to mortgagors in the exercise of its discretion under section 105. The benefits of the proposed exception to the automatic stay in section 362(b)(8) could thus be negated, if the bankruptcy court is free to exercise its power under section 105. Accordingly, the amendment to section 105 would prevent imposition of a discretionary stay on HUD and Agriculture in situations where, under the amendments proposed to section 362(b)(8), an automatic stay may not be imposed.

As noted above, this proposal would also expand the current exception in a further respect -- by extending the coverage that would be afforded to HUD's National Housing Act multifamily programs to hospital and nursing home programs under sections 242 and 232, respectively, of the National Housing Act; to Land Development programs under title X of the National Housing Act (as it existed immediately before the effective date of the Department of Housing and Urban Development Reform Act of 1989); to the section 312 multifamily Rehabilitation Loan program; to projects under section 202 of the Housing Act of 1959; and to any other projects with mortgages held or insured by HUD under existing or now-dormant programs; and to the Department of Agriculture's multifamily rural housing program. Thus, for these additional programs as well, the proposed amendments would ensure that the Secretaries of HUD and Agriculture have adequate and timely recourse against defaulting mortgagors, and would permit acts short of foreclosure (such as the Secretary of HUD or the Secretary of Agriculture taking possession or seeking appointment of a receiver). There seems to be no relevant basis upon which these additional programs should be distinguished from the National Housing Act multifamily programs for Bankruptcy Code purposes.

One technical item deserves mention. Under existing section 105, a bankruptcy court may not appoint a receiver, and that prohibition is carried into the proposed revision. Nonetheless, the proposal would permit the Secretary of HUD or Agriculture to appoint a receiver for the specific property involved. These provisions are not contradictory because of differences in who may appoint the receiver and the jurisdiction that the receiver may have, i.e., supervision of an affected property versus the estate of a bankrupt.

Under Secretary Dellibovi
Further Response to Rep. Carper

"Proportional accounting" refers to how CDBG funds spent by grantees would be credited for the purpose of meeting the requirement that a minimum percentage of funds (currently 60%, raised to 75% in the Administration's HUD Reform proposal) must be spent to benefit low- and moderate-income persons. For this purpose, the amount of CDBG funds spent on an activity that does not exclusively benefit low- and moderate-income persons would be discounted to the degree that the percentage of low- and moderate-income persons benefiting from the activity falls short of 100%.

For example, consider a grantee's expenditure of \$100,000 of CDBG funds for an economic development activity that creates 10 new jobs. Under the current statute and regulations, all \$100,000 would be counted toward meeting the grantee's overall requirement that 60% of its activities benefit low- and moderate income persons. Under the proposed approach, only 70% of the \$100,000, or \$70,000 would be credited toward meeting the overall benefit requirement.

There are two additional aspects of the proportional accounting proposal: the treatment of housing activities, and the potential for receiving credit for activities carried out under the national objectives of slums/blight treatment and urgent needs.

The 75% proportional accounting proposals are expected to require grantees to fund activities serving higher proportions of

lower income beneficiaries. This could be counterproductive in view of our national policy of avoiding undue concentrations of lower income persons in HUD-assisted housing projects.

Accordingly, special allowance would be provided so that CDBG expenditures on multifamily housing could receive full credit even when substantially less than 100% of the units would be occupied by lower income persons. This would be accomplished by requiring appropriate levels of non-CDBG contributions for such housing, so that the percent of total project development cost provided by CDBG does not exceed the percent of the units that are occupied by lower income persons.

Finally, under current law, an activity where the proportion of beneficiaries that are lower income falls just short of the threshold would not qualify under the national objective of benefiting low- and moderate-income persons, and therefore would not contribute at all to the require 60% overall benefit. This would be so even though the activity qualifies under another national objective. Under the proposed proportional accounting approach, however, such an activity could receive credit based on the level of demonstrable benefit to lower income persons. While the number of grantees that could make use of this feature would be limited (i.e. "distressed" communities), it would add an important dimension of flexibility.

Under Secretary DelliBovi
Further Response to Rep. Kennedy

Congressman, we agree with you that technical assistance funding serves an extremely useful function in promoting community economic development, and the Administration does not intend to "throw technical assistance out the window." Our proposal would earmark technical assistance funds to a broader variety of CDBG and other HUD program needs than is currently the case. It would broaden the number of subject areas covered by technical assistance and afford the Department the opportunity to coordinate HUD's housing and CDBG programs in a more rational manner.

The technical assistance would be made available on a competitive basis. Notices of funding opportunities would be published in the Federal Register and Commerce Business Daily and awardees would be selected on the basis of objective criteria established for each round. By utilizing the competitive process and publicizing the availability of funds and selection criteria to be used, the Department will eliminate opportunities for abuse and favoritism and serve the needs of program participants in a more cost-effective and equitable manner.

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